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Supreme Court of the United States

OCTOBER TERM, 1994

JOSEPH W. TEAGUE and HELEN B. TEAGUE, STEVEN ALLEN BARKER, RITA STRAHOWSKI, SWANNEE BECK, and KAREN PEREZ TUCKER, Lifetime Partners of PTL, As Representatives of a Nationwide Class consisting of 150,000 PTL Lifetime Partners and of 27,839 Persons Who Partially Paid for Lifetime Partnerships,

Plaintiffs - Petitioners

v.

JAMES O. BAKKER, DAVID A. TAGGART, AIMEE CORTESE, and DELOITTE, HASKINS & SELLS

Defendants - Respondents

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

I. Whether the Fourth Circuit Decision Determining the PTL Lifetime Partners' Right To Recover Their $160,000,000 of Investments, Which Dismisses Primary Liability Claims or Ignores Them, Conflicts with This Court's Decision in *Central Bank of Denver* on Securities Liability, by Overextending That Decision to Primary Liability and Making It Retroactive?

A. Whether Primary Liability Claims against PTL's Independent Auditors Are Barred by *Central Bank*, Which Barred Only Aiding and Abetting Claims?
B. Whether Claims against PTL's Directors and Officers, Based on Their Negligence in Permitting Securities Violations, Are Barred by *Central Bank*?
C. Whether the Decision in *Central Bank* Should Be Retroactive, in View of the Prior Unanimity of the Circuits?

II. Whether the Fourth Circuit Decision Effectively Immunizing PTL's Outside Auditors or Ignoring Claims Conflicts with This Court's Decisions on Accountant Liability in *Arthur Young*, *Reves I*, and *Central Bank of Denver* and Other Circuits, by Ignoring False Certification of PTL's Financial Statements and Implying Immunity for Accounting Firms?

A. Whether Auditors Are Immunized for Securities Liability, Contrary to *Arthur Young*, *Reves I*, and *Central Bank*?
B. Whether Auditors Are Immunized for RICO Liability, Contrary to the Statute and *Reves II*?

C. Whether Auditors Are Immunized for Fraud Liability, Contrary to *Arthur Young*?

III. Whether the Fourth Circuit Decision Undercutting Civil RICO Liability Conflicts with the Decisions of This Court and of Other Circuits, by Gutting the Distinction Between Civil and Criminal RICO, Conflicting with Recent Decisions that Involvement in Management and Ownership of Stock Are Not Necessary under § 1962(b), and Lifting the Interest Acquired and Reliance Standards to Unreachable Levels, So That No One Was Liable for PTL Fraud?

A. Whether Civil RICO Instructions Can Be Peppered with References to Crimes and Criminal Intent Requirements?
B. Whether § 1962(b) Can Be Bent To Require Stock Ownership (Which Is Impossible in a Nonprofit Organization) and To Require Involvement in Management (Which This Court Said Is Not Required, in *Reves II*)?
C. Whether § 1964(c) Can Be Interpreted To Require Reliance on Each RICO Participant and Aider, Even Though They Try To Act Behind the Scenes?

LIST OF PARTIES

The parties to the proceedings below were the plaintiff-petitioner PTL Lifetime Partner class (certified by the district court), and the defendant-respondents Jim Bakker, David Taggart, and Aimee Cortese, and the accounting firm Deloitte Haskins & Sells (now known as Deloitte Touche, and described by the panel as DH&S). Other parties to the proceedings below that were dismissed were Laventhol & Horwath and William J. Spears (dismissed automatically because of the firm's bankruptcy during trial); and Roe Messner a/k/a Ronald Messner, Messner Enterprises, and Commercial Builders of Kansas (dismissed voluntarily).

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INTRODUCTION

This is the case that determines who is liable for PTL's sale of over $160,000,000 of Lifetime Partnerships to small investors, and the destruction of the value of those Partnerships through various frauds.

The lower court opinion is very thorough in holding that PTL's Lifetime Partnerships were securities. However, it overextended this Court's securities decision in *Central Bank of Denver* when it went far beyond the aiding and abetting claims, to invalidate or ignore primary securities liability claims against PTL's accountants and negligence claims against PTL's directors and officers, and to immunize those accountants on RICO and fraud claims.

OPINION BELOW

The opinion below (Appendix I) is reported at 35 F.3d 978 (4th Cir. 1994). Related opinions uphold Jim Bakker's criminal conviction, *United States v. Bakker*, 925 F.2d 728,731-32 (4th Cir. 1991); approve settlement of the other accounting firm's liability for $45,000,000, *In re Laventhol & Horwath,* No. 90 B 13839 (S.D.N.Y. Bkry. Aug. 24, 1992); deny insurance coverage for nonnegligent acts of directors and officers, *Employers Reinsurance Corp. v. Teague,* 972 F.2d 339 (4th Cir. 1992); *see National Union Fire Ins. Co. v. Heritage Village Church*, No. C-C-90-150-M (W.D.N.C. filed 1990); and adjudicate PTL's bankruptcy, *Benton v. Bakker,* 92 B.R. 1000 (D.S.C.Bkry. 1988),

aff'd, No. 0:89-81-16 (D.S.C. Oct. 26, 1990), *aff'd*, 944 F.2d 901-02 (4th Cir. 1991).

JURISDICTION

Federal jurisdiction exists under 28 U.S.C. § 1331. The Fourth Circuit entered its opinion September 23, 1994, and denied rehearing October 18, 1994. This Court's jurisdiction is under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

This petition involves the Securities Exchange Act § 10(b) and Rule 10b-5 (15 U.S.C. § 78j(b)), RICO (18 U.S.C. §§ 1961-1964), and state statutes (N.C.G.S. §§ 75D-2, 1-52, 53-26.1, 53-35, 53-28A; S.C. Code § 27-32). These statutes are quoted in the appendix.

STATEMENT OF THE CASE

A. COURSE OF PROCEEDINGS

This lawsuit was filed by a class of more than 160,000 PTL Lifetime Partners, who each paid an average $1,000 for a PTL investment program. The defendants are PTL officers and directors and PTL's independent accounting firm. Primary securities claims were made against Jim Bakker and the accountants (Deloitte Haskins & Sells, or DH&S), and negligence in permitting securities violations was alleged against some directors and officers: Jim Bakker, Vice President David Taggart, and Director Aimee Cortese. The Lifetime Partners were certified as a nationwide class, and more than 150,000 (94%) remained in the class. (35 F.2d at 981-84, Appendix I.)

The trial court granted a directed verdict on securities claims on the sole ground that Lifetime Partnerships were not securities. (Appendix III.) The jury rendered a $129,000,000 verdict against Bakker for common law fraud. The other accounting firm, Laventhol & Horwath, filed for bankruptcy the day after the Lifetime Partners rested their case against it, and subsequently settled for $45,000,000. *In re Laventhol & Horwath,* No. 90 B13839 (S.D.N.Y.Bkry. Aug. 24, 1992).

The Fourth Circuit correctly held that Lifetime Partnerships are securities, and reversed the directed verdict that had been entered under securities law. However, it applied this Court's decision in *Central Bank* retroactively to aiding and abetting claims, it overextended that to dismiss the primary liability claims against the accountants and the negligence claims against directors and officers, or ignored them.

B. STATEMENT OF THE FACTS

1. PTL Lifetime Partnerships as Securities

Jim Bakker and PTL raised over $160,000,000 by selling "Lifetime Partnerships" for an average $1,000, to build hotels to be managed by PTL and its management company. These Partnerships were sold with promotional materials that said the Partnership "will appreciate in value, making it of greater value than at the time of its origination," and that the Partnership in fact already had appreciated to at least "$20,000" or even "$1,005,487." (35 F.2d at 988.) The promotional materials also said that the Partnership was an "investment,"

and that "[y]ou cannot find a better investment opportunity anywhere." (*Id.* at 984.) Finally, they noted that 50% of the hotel rooms would be rented commercially, because "[w]e have to made the funds up from people who are renting the other rooms," to provide free lodging to Lifetime Partners. (*Id.* at 988.) Thus, profit was promised by appreciation, investment value, and commercial rents. Some other facts showing Lifetime Partnerships to be securities were summarized in the decision. (*Id.* at 986-90.)

The Fourth Circuit held that "the district court erred in granting appellees' motion for a directed verdict on plaintiffs' federal securities fraud claim." (*Id.* at 991.) The court followed the holding that "it is not inappropriate that a promoter's offerings be judged as being what they were represented to be." *SEC v. C.M. Joiner Leasing Corp.*, 320 U.S. 344, 352-53 (1943).

2. Bakker's Fraud and Negligence

The promises failed, and the Lifetime Partners lost their entire $1,000 investments--over $160,000,000:

> Bakker promised television viewers that he would limit the sale of partnerships to ensure that each partner would be able to use the facilities annually. Appellant, however, *oversold* the partnerships. He promised, for instance, to limit the sale of Grand Hotel partnerships to 25,000 but actually sold 66,683. In addition, Bakker used relatively few of the funds solicited from the partners to construct promised facilities. In fact, of the proposed Heritage Village facilities, only the Grand Ho-

> tel and one bunkhouse were actually completed. Instead, Bakker used partnership funds to pay operating expenses of the PTL and to *support a lavish lifestyle*. This extravagant living included gold-plated fixtures and a $570 shower curtain in his bathroom, transportation in private jets and limousines, an air-conditioned treehouse for his children and an air-conditioned doghouse for his pets. This combination of overselling partnerships and diverting partnership proceeds meant that the overwhelming majority of the partners never received the lodging benefits Bakker promised them.

Teague, 35 F.3d at 982, quoting 925 F.2d at 731-32.

3. The Accountants' Primary Securities Violations

Bakker responded to questions by saying on television, in newspaper ads, and in mass mailings that "[w]e have been audited by Deloitte Haskins & Sells for many years," and that [o]ne of the big audit firms in America is in here all the time."

The accountants (DH&S) falsely certified PTL's financial statements, without any qualification, and covered up the fraud and negligence, as summarized at 8-11 *infra*. As the Fourth Circuit noted, DH&S "administered PTL's 'Executive Payroll Account' upon which checks transmitting salary and benefits to Bakker" for up to $1.9 million a year were drawn (35 F.3d at 982); "expurgated" a qualification from its auditor's report to cover up PTL's insolvency (*id.* at 983); and covered up the pending IRS audit of Bakker's private inurement while privately recognizing the "IRS exam will find private inurement [and] it'll go to court [and] we'll lose" (*id.* at 984). DH&S also

covered up PTL's securities violations after being told the "obvious legal issues involved are ... [t]he possibility of a securities offering," and covered up Bakker's flagrant oversales of Lifetime Partnerships. Thus, the Fourth Circuit acknowledged that "the record contains evidence which supports plaintiffs' various theories of aiding and abetting liability on the part of DH&S." (*Id.* at 994.)

REASONS FOR GRANTING THE WRIT

I. THE FOURTH CIRCUIT DECISION CONFLICTS WITH THIS COURT'S DECISION IN CENTRAL BANK OF DENVER ON SECURITIES LIABILITY, BY OVEREXTENDING THAT DECISION TO PRIMARY LIABILITY AND MAKING IT RETROACTIVE.

Central Bank of Denver, N.A. v. First Interstate Bank, 114 S.Ct. 1439 (1994), only required dismissal of aiding and abetting claims, and did not require or allow dismissal of primary liability claims and director negligence claims. The Fourth Circuit erroneously and grossly overextended *Central Bank,* or simply ignored the other claims,[1] and thereby impaired

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[1]The Fourth Circuit did not expressly affirm on the primary liability claims, but simply overlooked them and then referred to only the Bakker claims being remanded for trial. 35 F.3d at 991 ("we must affirm the district court's dismissal of plaintiffs' claim that DH&S aided and abetted Bakker's alleged federal securities fraud violation"); *id.* at 992 ("In summary, we reinstate plaintiffs' securities fraud claims under federal and state law against Bakker, but we affirm the dismissal of plaintiffs' federal and state securities fraud claims [only aiding and abetting

the ability of the PTL Lifetime Partners to recover their $160,000,000.

The Fourth Circuit was correct that securities claims were wrongly dismissed by a directed verdict for PTL's Jim Bakker, because the trial court erred in holding that Lifetime Partnerships were not securities.

However, because the securities claims against Bakker were wrongly dismissed, the securities claims based on primary liability were also wrongly dismissed against PTL's accountants, Deloitte Haskins & Sells (DH&S). For the same reason, the negligence claims based on negligently permitting securities violations were also wrongly dismissed against PTL directors and officers.[2] Yet the Fourth Circuit upheld that.

A. *Primary* Liability Claims against Accountants Who Commit Securities Fraud Are Not Barred by *Central Bank of Denver,* but the Fourth Circuit Grossly Overextended *Central Bank* To Ignore Primary Liability Claims against PTL's Accountants under § 10(b).

1. Primary Liability of the Auditors Was Alleged.

The Lifetime Partner class consistently alleged primary securities liability against DH&S. Those allega-

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claims were mentioned] against DH&S."). The same is true of the director and officer negligence claims.

[2]The district court recognized this in denying DH&S's and the directors' and officers' motions to dismiss, and their motions for summary judgment, on securities claims. The court then denied those parties' motions for directed verdict on primary securities liability and director-officer negligence, except that the motion was granted on whether there was a security at all.

tions fill 5 pages of the restated amended complaint (Appendix V), as well as of the original complaint.

2. Central Bank Permitted Auditor Primary Liability

This Court's decision in *Central Bank*, while overturning aiding and abetting liability, expressly noted that accountants may still be liable for primary securities violations under § 10(b) (114 S.Ct.at 1455):

> Any person or entity, **including a lawyer, accountant,** or bank, who employs a manipulative device or makes a material misstatement (or omission) on which a purchaser or seller of securities relies **may be liable as a primary violator** under 10b-5, assuming *all* of the requirements for primary liability under Rule 10b-5 are met. . . . In any complex securities fraud, moreover, **there are likely to be multiple violators** . . . .

Accord, Reves v. Ernst & Young, 494 U.S. 56 (1990).

Moreover, this Court in *Central Bank* did not restrict conspiracy liability under § 10(b). *E.g., Merrill Lynch, Pierce, Fenner & Smith v. Curran*, 456 U.S. 353, 394 (1982) (federal: "those persons who are participants in a conspiracy to manipulate the market in violation of those rules are also subject"); *Burns v. Gulf Oil Corp.*, 246 N.C. 266, 98 S.E.2d 339, 343-44 (1957) (N.C. conspiracy). Conspiracy liability of DH&S was alleged, and the Fourth Circuit should not have struck it out or ignored it under *Central Bank.*

3. DH&S Acts Support Primary Liability.

DH&S committed primary securities violations by its manipulative and deceptive acts, culminating with false and fraudulent certification of PTL's financial state-

ments. Some acts were noted by the Fourth Circuit:

> *DH&S administered PTL's "Executive Payroll Account"* upon which checks transmitting salary and benefits to Bakker and other PTL executives were drawn [for millions of unauthorized dollars]....
> The compensation, bonuses, and cash benefits paid to Bakker, Tammy and Dortch all came from the Executive Payroll Account managed, through mid-1985, by DH&S....
> A draft of DH&S's audit report . . . expressed concern over "whether PTL w[ould] be able to continue as a 'going concern' based on current assets of only [$]8.6 million against [$28.5 million in current liabilities." J.A. 2046. Such concern *[qualification], however, was expurgated from the report* before its issuance....
> A DH&S workpaper . . . states: "IRS exam will find private inurement [and] it'll go to court [and] we'll lose." J.A. 2148. DH&S did, in a note to its 1984 audit report, make reference to the fact that the IRS had commenced its own audit of PTL, although *no specific mention was made of the issue of private inurement.*[3]

(*Id.* at 981, 982, 983, 984.) This is only a tiny part of the evidence of DH&S's primary wrongdoing.

The district court similarly found the case against DH&S on these facts to be a "relatively close and difficult" case on fraud theories (common law fraud, RICO, and timeshare laws), as the Fourth Circuit noted twice. (*Id.* at 984, 985.) Before entering the directed verdict on the ground that Lifetime Partnerships were

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[3]That note was manipulative and deceptive, because it neither conveyed the very non-routine and menacing focus of the IRS audit, nor the potential "loss of tax exempt status [that] threatened to create huge tax liabilities and to leave PTL unable to attract the deductible contributions which were its lifeblood."

not securities, the district court ruled that the securities primary liability claims against DH&S otherwise stated a claim, and were sufficient to weather summary judgment and the motion for directed verdict.

DH&S, when it certified PTL's financial statements, did so fraudulently and knowingly participated in Bakker's fraud, as DH&S's own workpapers showed:

a. Administering the Secret Payroll Account for Massive Looting. DH&S admitted that "executive payroll checks were written by DH&S based upon mgmt's authorization to protect the confidentiality of payroll amounts"--which was indeed essential to keep Bakker's looting secret and possible. DH&S prepared the checks for Bakker to pocket up to $1.9 million a year, and hid its $92,820 charge by naming it a "tax service." DH&S also prepared Bakker's personal tax returns, and was paid for a special study of his private inurement. DH&S continued this "tax service" until mid-1985, when PTL was insolvent and Partnerships were grossly oversold.

b. Covering Up PTL's Tax Exemption Loss. DH&S admitted (in its workpapers) knowing that "IRS exam will find private inurement and it'll go to court, [and] we'll lose." Yet DH&S drafted a footnote to the 1994 audited financial statements that misrepresented the IRS audit, and withheld a qualification about PTL's impending loss of tax exemption. Yet DH&S admitted knowing the "probability of an unasserted claim against PTL's tax-exempt status" and the "likelihood that the IRS may raise an issue as to private inurement" (as it

admitted in workpapers). DH&S in fact wrote Bakker's checks, prepared his tax returns, and did a private inurement study, before its 1984 or 1983 certifications. DH&S similarly concealed in the 1983 certification its knowledge of an IRS audit and that "one of the primary issues of the audit [was] private inurement."

c. Covering Up PTL's Insolvency (Going Concern Problem). DH&S admits that it initially qualified its certification for "whether PTL will be able to continue as a `going concern' based on current assets of only 8.6 million against 28.5 million in current liabilities," and "chang[ed] the opinion" and destroyed that qualification under PTL pressure. Yet looking at the same records, PTL's vice president of finance issued weekly warnings that "[e]ach day brings us into a deeper crisis."

d. Covering Up Diversion of Lifetime Partner Funds. DH&S covered up the diversion of well over half of the Lifetime Partner investments from hotel construction to Bakker's compensation and other unauthorized purposes, by secretly preparing the checks for Bakker and not disclosing the massive transfers.

e. Covering Up Violations of Securities Laws. DH&S hosted a meeting to plan the first Lifetime Partnership soliciation, where it heard PTL's tax counsel note that the "obvious legal issues involved are . . . [t]he possibility of a securities offering," and heard him advise against mailing the Partnership solicitation. DH&S had a copy with promises that "[y]ou cannot find a better investment opportunity anywhere," and

that the value was "almost $20,000!" DH&S ignored its duty to inquire, and covered up the violations.

f. Covering Up Oversales of Lifetime Partnerships. DH&S knew about the flagrant oversales, and covered them up, as ample evidence shows.

DH&S's false certification of PTL's financial statements was essential for Bakker's fraud to succeed, because Bakker advertised to the Lifetime Partners that PTL was financially squeaky clean because "[w]e have been audited by Deloitte Haskins & Sells for many years" and "[o]ne of the big audit firms in America is in here all the time," in television, newspapers, and mailings.

4. Other Circuits Find Primary Liability in Such Acts

DH&S's actions are more manipulative and deceptive than those of other auditors whose cases have involved primary violations of securities laws.[4]

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[4] *E.g.*, Bradford-White Corp. v. Ernst & Whinney, 872 F. 2d 1153, 1159 (3d Cir. 1989) ("The crux of this finding of liability is that Ernst & Whinney failed to conduct an audit of Jackson which complied with GAAS but that it nonetheless represented [certified] that it had complied with GAAS."); Rudolph v. Arthur Andersen & Co., 800 F.2d 1040, 1043, 1044 (11th Cir. 1986) (primary liability potential from audits and nonaudit services by not "tak[ing] reasonable steps to correct misstatements they have discovered in previous financial statements," and not "disclos[ing] actual knowledge of fraud"); James v. Meinke, 778 F.2d 200, 202 (5th Cir. 1985) (primary liability verdict affirmed under Rule 10b-5 when accountant "did not fully disclose Bratton's financial status and prospects before they bought their stock"); United States v. Weiner, 578 F.2d 757, 782, 784 (9th

As indicated in these cases, DH&S had a duty not to issue a false or misleading certification, in certifying PTL's financial statements. *Accord, United States v. Arthur Young & Co.*, 465 U.S. 805, 817-18 (1984) ("By certifying the public reports . . ., the independent auditor assumes a public responsibility . . . . This 'public watchdog function' . . . requires complete fidelity to the public trust."); *United States v. Benjamin*, 328 F.2d at 863 (2d Cir. 1964) ("In our complex society the accountant's certificate . . . can be instruments for inflicting pecuniary loss more potent than the chisel or the crowbar.").

B. Negligence Claims against Directors and Officers Who Permit Securities Violations Are Not Barred by *Central Bank of Denver*, but the Fourth Circuit Grossly Overextended *Central Bank* To Ignore Claims against PTL's Directors and Officers Who Permitted § 10(b) Violations.

Cir. 1978), *cert. denied*, 439 U.S. 981 (1979) (auditors "knowingly and willfully made or caused to be made false and misleading statements in the auditor's report"; "The overwhelming scope of the fraud, its often complex but sometimes very simple mechanisms, and the failure of the auditors to find in any of the suspicious procedures cause to dig further into Equity Funding's financial records system all lead to the inescapable conclusion that defendants [auditors] were involved."); United States v. Natelli, 527 F.2d 311, 323-24, 319, 321 (2d Cir. 1975) (auditor "culpable if he acted in `reckless disregard' of the facts or if he `deliberately closed his eyes'" to fraud, or had a "failure to make open disclosure" and "concealment of retroactive adjustments"); Competitive Associates, Inc. v. Laventhol, Krekstein, Horwath & Horwath, 516 F.2d 811, 813 (2d Cir. 1975) (auditor "knowingly and with intent to defraud certified these statements in order to facilitate, aid and abet Yamada's scheme").

The *Central Bank* decision similarly does not eliminate negligence claims against directors and officers for permitting securities fraud. Thus, the gross negligence claims against PTL directors and officers for permitting these securities violations, and for violating North Carolina securities law, remain viable, were wrongly dismissed by the trial court in its directed verdict, and should also go back to trial along with the primary securities claims against Bakker and DH&S. These negligence claims were wrongly struck by the Fourth Circuit opinion under an overextension of *Central Bank,* or wrongly ignored.

These gross negligence claims are vitally important to the Lifetime Partner class, because they allow recovery for the victims from the insurers of much of the $160,000,000 lost by the Lifetime Partners.[5]

1. Negligence Liability of Directors and Officers for Permitting Securities Violations Was Alleged

Gross negligence claims for permitting securities violations were made against Bakker, Taggart, and Cortese in the restated amended complaint and in the second amendment (quoted in Appendix V, § 440B).

Negligence in violating the North Carolina securities provision (N.C.G.S. § 78A-8) may be actionable.

[5]The National Union Insurance policy involves approximately $35,000,000, and the Employers Reinsurance policy involves well over $30,000,000, in coverage, which in turn would reduce the exposure for DH&S. *See* National Union Fire Ins. Co. v. Heritage Village Church & Missionary Fellowship, No. C-C-90-150 (W.D.N.C. filed *, 1990); Employers Reinsurance Corp. v. Teague, 972 F.2d 339 (4th Cir. 1992).

The Fourth Circuit noted the issue is unresolved. (35 F.3d at 992.) That claim comes within the negligence allegations against Bakker, Taggart, and Cortese.

2. Central Bank Permitted D&O Negligence Liability.

Central Bank does not conflict with the liability of directors and officers for negligence in, among other things, permitting securities violations. The Fourth Circuit overextended it, or ignored the claims.

3. The Directors' and Officers' Acts Support Gross Negligence Liability.

PTL officers were warned (in DH&S's offices), before the first Lifetime Partnership promotion was mailed, that the "obvious legal issues involved are . . . [t]he possibility of a securities offering." They then were warned not to mail the Lifetime Partnership promotion, by PTL's general legal counsel. They negligently supervised the largest securities violation in the history of religious organizations.

Bakker, after that warning, sold over $160,000,000 of Lifetime Partnerships in violation of securities law

Taggart thereafter cancelled a halt to oversales of Lifetime Partnership securities, and was aware of the oversales. He was the second-highest paid official at PTL, and the third-ranking officer of PTL as "Vice President of Executive Offices."

Cortese as well as Taggart received the promotional materials for Lifetime Partnerships, which promised that "[y]ou cannot find a better investment opportunity anywhere . . . . worth almost $20,000" and that Towers

Partnerships were "literally worth hundreds of thousands of dollars." She did nothing to stop, or ask about, securities sales, or securities violations by oversales (despite knowing the limits),[6] even though she received PTL's financial statements and received $15,000 a year as a director. The trial judge's conclusion at the time (though he found Cortese's nonliability more compelling six months after trial) was:

> It may be a close case whether she is guilty of gross negligence or not. . . .
> The evidence, I believe, shows, if anyone wishes to find it, that it would support a finding of ordinary negligence.

The bankruptcy judge similarly found Cortese and the other directors grossly negligent. *Benton v. Bakker,* 92 B.R. 1000, 1016 (D.S.C. Bkry. 1988).

The district court similarly ruled that the negligence claims for permitting securities violations stated a claim, and were sufficient to weather summary judgment and the motion for directed verdict.

C. *Central Bank of Denver* Should Not Be Made Retroactive, in View of the Circuits' Unanimity Beforehand, but the Fourth Circuit Made *Central Bank* Retroactive Even though It Was Unforeseeable.

The uniform decisions of all eleven circuits on Section 10(b) aiding and abetting were overturned by *Central Bank* in April 1994. Thus, the rule in

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[6] She similarly did nothing to stop, or ask about, mind-boggling compensation, tax exemption loss, or fund diversions. She approved $3.4 million in bonuses to the Bakkers.

Central Bank could not be reasonably foreseen. This case was filed six years *before* that, with aiding and abetting claims along with primary liability claims, and went to trial four years before *Central Bank*, when all circuits supported aiding and abetting liability. Thus, *Central Bank* should not apply retroactively to this and similar cases.

II. THE FOURTH CIRCUIT DECISION CONFLICTS WITH THIS COURT AND WITH OTHER CIRCUITS ON ACCOUNTANT PRIMARY LIABILITY, BY IGNORING FALSE CERTIFICATION OF PTL'S FINANCIAL STATEMENTS, AND BY IMPLYING IMMUNITY FOR ACCOUNTING FIRMS.

This Court has not fully addressed an accountant's liability for falsely certifying financial statements. However, it has acknowledged the auditor's high responsibility as a "public responsibility" and "'public watchdog' function," and has given reasons against "insulat[ion] from disclosure" that equally apply against insulation from liability. The Fourth Circuit, to the contrary, implied auditor immunity.

> By certifying the public reports that collectively depict a corporation's financial status, the independent auditor assumes a *public* responsibility transcending any employment relationship with the client. The independent public accountant performing this special function owes ultimate allegiance to the corporation's creditors and stockholders, as well as to the investing public. This "public watchdog" function demands that the accountant maintain total independence from the client at all times and requires complete fidelity to the public trust. To insulate from disclosure [pursuant to an IRS summons] a certified public accountant's inter-

> pretations of the client's financial statements would be to ignore the significance of the accountant's role as a disinterested analyst charged with public obligations.

United States v. Arthur Young & Co., 465 U.S. 805, 817-18 (1984).[7]

This case against the independent auditors (DH&S) was a "relatively close and difficult" case on the non-securities fraud theories (RICO, common law fraud, and timeshare laws), as the district court found at the end of a seven week trial, and as the Fourth Circuit twice noted. (35 F.3d at 985, 996.) "[T]he record contains evidence which supports plaintiffs' various theories of aiding and abetting liability on the part of DH&S," as the Fourth Circuit acknowledged. (*Id.* at 994.) The jury would likely have found DH&S liable if the district judge had not erred on several points, and those errors would have been reversed if the Fourth Circuit had not treated the auditors as effectively immune from the $129,000,000 liability.

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[7] *See also* AU 110.01 (giving a correct certification opinion is the "objective of the ordinary examination of financial statements by the independent auditor"); AU 410.01 (giving such an opinion is the "first standard of reporting" by auditors); AU 509.09(c) (auditor may not give the usual certification if the "financial statements are affected by a departure from a generally accepted accounting principle"); AU 509.15 (instead "should express a qualified or an adverse opinion"); AU 509.17 ("should express a qualified or an adverse opinion" if there is "inadequate disclosure"). AU refers to Auditing Standards Board, *Codification of Statements on Auditing Standards.*

A. Securities Immunity for Auditors' Primary Violations Is Contrary to *Arthur Young, Reves I,* and *Central Bank of Denver,* but the Fourth Circuit Ignored the Auditors' False Certification of PTL's Financial Statements and Implied Immunity for Accounting Firms.

1. Effective Immunization of the Auditors

The trial court dismissed all securities claims on the erroneous ground that Lifetime Partnerships could not be securities, and thereby dismissed the primary liability claims against DH&S, as discussed in I *supra.* The Fourth Circuit reversed the former, but either upheld or ignored the latter, which had the effect of immunizing the auditors from securities liability for their primary violations.

2. Conflict with This Court and Other Circuits

That Fourth Circuit approach conflicts with *Arthur Young & Co.*, which implied auditor liability for falsely certifying financial statements, and *Reves v. Ernst & Young,* 494 U.S. 56 (1990), which upheld auditor liability for false certification. It also comflicts with *Central Bank of Denver,* which said that an "accountant . . . who . . . makes a material misstatement (or omission) . . . may be liable as a primary violator under 10b-5." The Fourth Circuit approach also conflicts with the decisions of other circuits, which hold auditors liable for primary securities violations (citations in I.A.4 *supra*). DH&S's false certification of PTL's financial statements and other primary acts were comparable to the primary secu-

rities violations in those cases.

B. RICO Immunity for Auditors' Violations of RICO Is Contrary to that Statute and to the *Reves II* Decision, but the Fourth Circuit Ignored the Auditors' False Certification of PTL's Financial Statements and Implied Immunity for Accounting Firms.

1. Effective Immunization of the Auditors

The Fourth Circuit upheld the trial court's instructions that the auditors, to be liable under *civil* RICO, must have had "specific *criminal* intent" as aiders and abettors or "*criminal* intent as conspirators. The Fourth Circuit also upheld criminal requirements for the primary RICO violators, and a stock ownership requirement that could not be met by PTL insiders. Those requirements effectively immunized the auditors. They are discussed in III *supra*.

2. Conflict with This Court and Other Circuits

That Fourth Circuit approach conflicts with *Arthur Young & Co.*, which implied accountant liability for falsely certifying financial statements, and with *Reves II,* which held auditors potentially subject to RICO liability. *"'[O]utsiders'* may be liable under § 1962(c) if they are 'associated with' an enterprise and participate in the conduct of its affairs," and "the 'operation or management' test that applies under subsection (c) in no way limits the application of subsections (a) and (b) to *'outsiders.'"* *Reves v. Ernst & Young*, 113 S.Ct.1163, 1173 (1993). It also conflicts with *Sedima* and other recent RICO decisions, which strike down judicial hurdles to RICO

verdicts. *E.g., Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479 (1985). The Fourth Circuit approach also conflicts with the decisions of other circuits, holding auditors liable for RICO violations.[8]

C. Common Law Fraud Immunity for Auditors' Violations and Aiding and Abetting Is Contrary to *Arthur Young* and to State Statutes, but the Fourth Circuit Ignored the Auditors' False Certification of PTL's Financial Statements and Implied Immunity for Accounting Firms.

1. Effective Immunization of the Auditors

The Fourth Circuit upheld the trial court's jury instructions that (repeatedly) gave the statute of limitations as an absolute 3-year period without any equitable tolling (tolling should have occurred, N.C.G.S. § 1-52(9), because fraud prevented discovery of Bakker's and DH&S's wrongdoing). The appeals court's only expla-

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[8] *E.g.*, James v. Meinke, 778 F.2d 200, 202 (5th Cir. 1985) (jury verdict affirmed convicting accountant of RICO and Rule 10b-5 primary violations when "did not fully disclose Bratton's financial status and prospects before they bought their stock"); Schacht v. Brown, 711 F.2d 1343, 1345 (7th Cir. 1983) (RICO claim stated against accounting firm that "knew of Reserve's insolvency" and "prepared unqualified opinion letters"); *see* Emrich v. Touche Ross & Co., 846 F.2d 1190 (9th Cir. 1988) (RICO claims stated against auditor); Penturelli v. Spector, Cohen, Gadon & Rosen, 779 F.2d 160 (3d Cir. 1985) (same); Bennett v. Berg, 685 F.2d 1053 (8th Cir. 1982) (same in connection with failed nonprofit retirement village interest); *see* Bank of America National Trust v. Touche Ross & Co., 782 F.2d 966, 971 (11th Cir. 1986) (RICO claim stated against accountant for "prepar[ing] false financial statements and reports") (modified in *Reves*).

nation was the cryptic conclusion without any citation that "[t]he record refutes this argument,"[9] and the trial court had actually acknowledged the error and agreed to reinstruct the jury (then declined to). The appellate court also conceded that a statute of limitations instruction was totally unnecessary, because "no Lifetime Partners were aware of PTL's financial difficulties" until within 3 years of filing suit, and yet without explanation summarily found "no prejudicial error." (35 F.3d at 994n.22.) The absolute 3-year period left Bakker on the hook (he continued running PTL until 1/2-year before suit was filed), but let DH&S off the hook (it completed its audit just over 3 years before suit was filed).[10] The jury predictably found Bakker liable for $129,000,000, but DH&S not liable for fraud, taking the instruction literally. This effectively immunized DH&S from fraud liability. Yet the Fourth Circuit recognized "the record contains evidence

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[9]The jury clearly applied the 3 year date before suit as an absolute bar, because it subtracted from the total Lifetime Partner losses ($161,482,763) the Lifetime Partnership sales as of the 3 year date before suit was filed ($31,815,523 on November 17, 1984), and set damages at $129,667,240. However, with equitable tolling, that $31,815,523 should have been included, and DH&S (which had finished its audit before that 3-year date) should have been liable.

[10]The instructions similarly let DH&S off the NCRICO hook by erroneously requiring not just that one defendant commit an act after October 1986, but that each defendant do so. N.C.G.S. § 75D-3(b). They also wrongly used the reasonable doubt standard for NCRICO, and wrongly used the absolute 3-year bar for the time share claims.

which supports plaintiffs' various theories of aiding and abetting liability on the part of DH&S." (*Id.* at 994.)[11]

2. Conflict with This Court and Other Circuits

That Fourth Circuit immunity conflicts with this Court's statement on auditor responsibilities in *Arthur Young,* and with other circuits' decisions on auditor liability for fraud. DH&S's actions compare darkly with those of other auditors that have committed primary violations of fraud laws.[12]

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[11] The Fourth Circuit's straining to immunize auditors is also evident in its finding that Lifetime Partnerships did not meet the definition of a "vacation time sharing plan" under South Carolina law, although the definition was otherwise a perfect match, for the sole reason that one or more Lifetime Partners might not live at least a year. (Two of 160,000 died during the first year of the program.) 35 F.3d at 993. Thus, there was no timeshare fraud, or DH&S fraud liability.

[12] *E.g.*, North River Insurance Co. v. Stefanou, 831 F.2d 484, 485-86 (4th Cir. 1987) (auditor's fraud and conspiracy to create fraudulent tax deductions); Rudolph v. Arthur Andersen & Co., 800 F.2d 1040, 1043, 1044 (11th Cir. 1986) ("Such a duty may exist `where the law imposes special obligations, as for auditors, . . . depending on the circumstances of the case.'"; "Standing idly by while knowing one's good name is being used to perpetuate a fraud is inherently misleading" "where the issue is disclosure of actual knowledge of fraud."; "`duty is to safeguard the public interest,' to disclose fraud in this type of circumstance") (primary fraud liability); Bank of America National Trust v. Touche Ross & Co., 782 F. 2d 966, 970 (11th Cir. 1986) ("assist[ed] in the preparation and dissemination of false financial statements") (primary RICO liability); Admiralty Fund v. Hugh Johnson & Co., 677 F.2d 1301, 1313 (9th Cir. 1982) (fraud); United States v. Natelli, 527 F.2d 311,

III. THE FOURTH CIRCUIT DECISION CONFLICTS WITH THIS COURT AND WITH OTHER CIRCUITS ON CIVIL RICO LIABILITY, BY GUTTING THE CIVIL-CRIMINAL DISTINCTION, AND BY IGNORING THIS COURT'S RECENT DECISIONS ON THE ACQUISITION OF INTEREST AND RELIANCE STANDARDS, LIFTING THEM TO UNREACHABLE LEVELS.

This Court has never fully delineated what portions of civil RICO must remain civil, not criminal. However, it has held that civil RICO does not require organized crime, criminal convictions, or crimes.

The Fourth Circuit upheld, in analysis limited to a footnote, the trial court heavily peppering the *civil* RICO jury instructions with *criminal* language, and requiring *"stock or ownership equity"* for § 1962(b)-(c) liability in a nonprofit organization. These improper constructions frustrate civil RICO.

323-24, 319, 321 (2d Cir. 1975) ("culpable if ... `deliberately closed his eyes'" to fraud, or had a "failure to make open disclosure" and "concealment of retroactive adjustments"); Competitive Associates, Inc. v. Laventhol, Krekstein, Horwath & Horwath, 516 F.2d 811, 813 (2d Cir. 1975) ("knowingly and with intent to defraud certified these statements in order to facilitate, aid and abet Yamada's scheme"); United States v. Simon, 425 F.2d 796, 806-07 (2d Cir. 1969), *cert. denied*, 397 U.S. 1006 (1970) ("If certification does not at least imply that the corporation has not been looted by insiders so far as the accountants know, . . . it would mean nothing") (primary fraud liability); United States v. Benjamin, 328 F.2d 854, 863 (2d Cir.), *cert. denied* sub nom. Howard v. United States, 377 U.S. 953 (1964) ("members of these ancient professions should not be able to escape criminal liability on a plea of ignorance when they shut their eyes to what was plainly to be seen") (primary fraud); United States v. White, 124 F.2d 181 (2d Cir.1941).

A. Crimes and Criminal Intent Are Not Required To Violate Civil RICO, as This Court Said in *Tafflin* and Intimated in *Sedima* in Questioning Whether Criminal Burdens Apply, but the Fourth Circuit Upheld *Criminal* Standards for *Civil* RICO.

The jury instructions in this civil RICO case required proof of criminal acts, criminal intent, and the criminal reasonable doubt standard. The Fourth Circuit upheld the instructions. The jury instructions consistently described the necessary racketeering acts as "crimes" and "criminal" acts. The same was true of the North Carolina RICO instructions. For example, the following instruction was read and then repeated:

> Racketeering acts or predicate acts are **crimes**, and in the RICO statute, Congress listed a number of times what can be predicate acts. The list includes both Federal law **crimes** and state law **crimes**. Congress deliberately made the list broad with the intent of including all kinds of **criminal** activity in which organized **crime** was or could be involved. The listed **crimes** are referred to as predicate acts because the RICO violation is predicated or dependent upon proof that someone committed these **crimes**.

The instructions required criminal intent: "specific intent to defraud," a primary violator to be "convicted" and "guilty," "criminal intent" for conspirators, "specific intent" for aiders and abettors to be liable, and "specific criminal intent" for aiders and abettors under state RICO. The instructions used the criminal aiding and abetting standard, and required proof beyond a reasonable doubt for state RICO.

1. No Crime Requirement under Federal Civil RICO.

a. No Criminal Claim. This Court recognized that "civil" RICO claims do not require "crimes": "civil RICO claims are not `offenses against the laws of the United States,' § 3231, and do not result in the imposition of criminal sanctions." *Tafflin v. Levitt,* 493 U.S. 455, 464 (1990). "The word `conviction' does not appear in any relevant portion of the statute." *Sedima, S.P.R.L. v. Imrex Corp.,* 473 U.S. 479, 488 (1985). This Court also differentiated between "criminal purposes" and "legitimate business" to say that the RICO enterprise need not be criminal and could be non-criminal. *H.J., Inc. v. Northwestern Bell Telephone Co.,* 492 U.S. 229, 242-43 (1989). And the Court rejected arguments that civil RICO liability requires organized crime[13] or criminal conviction.[14]

The text of RICO itself, as a statute with civil and criminal uses, carefully refers to "racketeering activity," "acts", and "predicate acts" rather than "crimes."[15]

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[13]492 U.S. at 236-37, 244-45; United States v. Turkette, 452 U.S. 576, 587 (1981). The Court's reasons for rejecting an organized crime requirement, 492 U.S. at 244, apply equally to any crime requirement.

[14]Sedima, 473 U.S. at 493, *rev'g,* 741 F.2d 482 (2d Cir. 1984). The Court's reasons for rejecting a conviction requirement, 473 U.S. at 488, apply equally to a crime requirement.

[15]18 U.S.C. §§ 1961(1) (definition of racketeering activity), 1961(5) (definition of

b. No Criminal Standard of Proof. Moreover, the RICO standard of proof is not the criminal law reasonable doubt test, but the civil preponderance test:

> In a number of settings, conduct that can be punished as criminal only upon proof beyond a reasonable doubt will support civil sanctions under a *preponderance standard.* [Citations omitted.] There is no indication that Congress sought to depart from this general principle here. . . . But we need not decide the standard of proof issue today.

Sedima, 473 U.S. at 491. All circuits agree.

c. No Criminal Intent. Civil RICO does not require criminal intent; "That the offending conduct is described by reference to criminal statutes does not mean that its occurrence must be established by criminal standards." *Id.*

2. No Crime Requirement under North Carolina Civil RICO.

The same is true under North Carolina RICO (NCRICO), which expressly says it "constitutes a civil offense only and *is not a crime*," and does not require "criminal intent." N.C.G.S. §§ 75D-4(b).

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pattern), 1962 (prohibited activities), 1964(c) (civil action). *Accord*, Sedima, S.P.R.L. v. Imrex Corp., 473 U.S. at 488 ("[Section 1964(c)] refers only to a failure to adhere to legal requirements [a violation]. . . . Section 1962 renders certain conduct `unlawful; § 1963 and § 1964 impose consequences, criminal and civil, for `violations' of § 1962."); Blakey & Cessar, *Equitable Relief Under Civil RICO,* 62 Notre Dame L. Rev. 526, 530 n.14 (1987) (RICO's draftsman) ("Section 1962, in short, states what is `unlawful,' not `criminal.'").

B. Stock Ownership and Management Involvement Are Not Required To Violate Civil RICO § 1962(b), as This Court Has Recently Held, but the Fourth Circuit Upheld Those Requirements, Which Could Never Be Met in a Nonprofit Organization Such as PTL or by Outside Auditors for PTL.

1. No Stock Ownership Requirement for § 1962(b)-(c)

This Court recently held that a "'profit-seeking' entity" is "not required" for RICO liability. *National Organization for Women v. Scheidler,* 510 U.S. ___, 127 L.Ed.2d 99, 109 (1994). This Court also has defined "interest" broadly under RICO § 1962(b). *Russello v. United States,* 464 U.S. 16, 21 (1983).[16] The trial court and Fourth Circuit contradicted that by a "stock ownership" requirement for § 1962(b)-(c) liability.

The jury instructions said that employment could never constitute the "interest" in the enterprise that RICO and NCRICO require, and that only stock ownership (which was not possible in connection with PTL) could meet the "interest" requirement of RICO §§ 1962(b)-(c). RICO liability could be evaded if the violator were smart enough to work through a nonprofit organization, as Bakker did with PTL. The instructions let Bakker off the RICO and NCRICO hook, and without a primary violator they let DH&S and Taggart off the hook too. Also, the lower court's instruction did not limit itself to § 1962(b), and left the confusing impression

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[16] *Accord,* Riverwoods Chappaqua Corp. v.Marine Midland Bank, RICO Bus.Dis. Guide §8610 (2d Cir. 1994).

that employment could not constitute any of the prohibited conduct under RICO § 1962(c) either, even though § 1962(c) expressly includes"employ[ment]."

The "stock ownership" requirement conflicts with RICO's text and with the Seventh Circuit. § 1962(b) does not limit itself to "stock or ownership," or disqualify "employment" from the interest "acquire[d] or maintain[ed]." To the contrary, § 1962(b) covers employment by broad reference to "any interest in" and to "control" of the enterprise, as well as by reference to "indirectly." The Seventh Circuit expressly defined "control" in 1962(b) not to require stock ownership. *Sutliff, Inc. v. Donovan Companies,* 727 F.2d 648, 653 (7th Cir. 1984). The other circuits' decisions holding that the "person" need not be different from the "enterprise" under § 1962(a)-(b) are effectively saying the same thing.

The exclusion of nonprofit organizations conflicts with RICO's text and this Court's decision. § 1962 covers nonprofit organizations, because the definition of "enterprise" in § 1961(4) is equally broad, as the Court held in *National Organization for Women.*

2. No Involvement in Management Test for § 1962(c).

The Fourth Circuit upheld these instructions, by incorrectly equating the clear "stock ownership" language with an *unrelated* requirement in the instructions for "involvement in the management and operation of PTL." (35 F.2d at 995 n.23.)

However, that justification contradicted this

Court's pronouncement on § 1962(b) liability, that "the 'operation or management' test that applies under subsection (c) in no way limits the application of subsections (a) and (b) to 'outsiders.'" *Reves v. Ernst & Young*, 113 S.Ct.1163, 1173 (1993). Thus, the Fourth Circuit's only misjustification for the erroneous "stock ownership" requirement under § 1962(b) was an equally erroneous "involvement in management" requirement that hindered § 1962(b) liability.

These points equally apply to NCRICO, which has virtually identical language.

C. Reliance on Each Defrauder Is Not Required to Violate Civil RICO § 1964(c), and Could Not Be Met When Defrauders Act Behind the Scenes, Aid and Abet, or Conspire, but the Fourth Circuit Required Reliance on Not Just One but on Each Participant for RICO Liability.

The Fourth Circuit has read into RICO a requirement for reliance on each participant, not just on the primary wrongdoer. *Brandenberg v. Seidel,* 859 F.2d 1179, 1188 n.10 (4th Cir. 1988) ("such reliance is necessary to establish injury to business or property 'by reason of' a predicate act of mail fraud within the meaning of § 1964(c)"). That is precisely the sort of judicial hurdle to RICO that this Court keeps condemning.

CONCLUSION

Thus, we request that certiorari be granted.

Dated December 23, 1994 and respectfully submitted,

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APPENDIX

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FOURTH CIRCUIT OPINION

U.S. COURT OF APPEALS FOR THE FOURTH CIRCUIT

NO. 91-2101, -2120, -2121

[STYLE OMITTED]

(Decided: September 23, 1994)

Affirmed in part; reversed and remanded in part.

Before RUSSELL and HALL, Circuit Judges, and CLARKE, Senior United States District Judge for the Eastern District of Virginia, sitting by designation.

Affirmed in part and reversed and remanded in part by published opinion. Judge DONALD RUSSELL wrote the opinion, in which Judge K.K. HALL and Senior Judge CLARKE joined.

RUSSELL, Circuit Judge:

The plaintiffs, members of a class of approximately 160,000 individuals who purchased "Lifetime Partnerships" from an entity known as "PTL" entitling them to a short stay annually in a hotel at a vacation retreat constructed by PTL, brought the instant suit against numerous defendants alleging common law fraud, federal and state securities fraud, state timeshare fraud, federal and state RICO violations, and negligence, all in

connection with the oversale of PTL Lifetime Partnerships. Plaintiffs proceeded to trial against James O. Bakker ("Bakker"), Deloitte, Haskins & Sells ("DH & S"), Aimee Cortese ("Cortese") and David A. Taggart ("Taggart"). Before the case was sent to the jury, the district court granted defendants' motion for a directed verdict with respect to plaintiffs' securities fraud claims. Following deliberations, the jury found Bakker guilty only of common law fraud. DH & S, Taggart and Cortese were absolved of all liability. The district court entered judgment against Bakker on the common law fraud count for $129,618,000 in compensatory damages and for an additional $129,618,000 in punitive damages. Plaintiffs appeal from the judgments entered against them. Bakker cross-appeals on the ground that the issues of reliance, causation and damages in relation to the adverse fraud verdict should have been handled on an individual class member basis. DH & S and Taggart cross-appeal from the district court's denial of their petition for reimbursement of costs. We reverse the district court's grant of judgment as a matter of law against plaintiffs on their securities fraud claims against Bakker, and otherwise affirm the district court's judgments in all respects.[1]

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[1]Prior to oral argument, DH & S made a motion to supplement the record. That motion is denied.

I.

A.

PTL, which stands for "Praise the Lord" and "People that Love," consists of various nonprofit entities. Bakker was the founder, president, a director, and the spiritual and financial leader of PTL. DH & S, an international accounting firm, provided PTL with independent auditing services in the early 1980's. DH & S's last audit of PTL was completed by October 24, 1984. In addition, during the time that it provided auditing services and for a time thereafter, DH & S administered PTL's "Executive Payroll Account" [*982*] upon which checks transmitting salary and benefits to Bakker and other PTL executives were drawn.

Cortese was the pastor of a small church in New York City. In 1979, a director of PTL, Reverend Richard Dortch ("Dortch"), approached Cortese about the possibility of Cortese joining PTL's board of directors. In 1980, despite her lack of experience with financial matters, Cortese agreed to serve on PTL's board. She remained a board member until 1987.

Taggart held various offices in PTL, including the title of vice-president, but he had few, if any, real management duties. Taggart was primarily Bakker's administrative aide and was not a PTL director.

This case concerns primarily PTL's sale of Lifetime Partnerships ("LTPs").[2] We previously affirmed

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[2]As described just below, PTL offered various

criminal convictions against Bakker arising therefrom. *United States v. Bakker*, 925 F.2d 728 (4th Cir.1991). At the time, we summarized the relevant underlying facts thus:

... [I]n the late 1970s PTL began construction on "Heritage USA," described by PTL officials as a Christian retreat center for families. In 1983, Bakker announced plans to enlarge the center by adding a vacation park, "Heritage Village," that would include the 500-room Grand Hotel. Between 1984 and 1986, [Bakker] announced further proposals to expand the Village by constructing the Towers Hotel, 50 bunkhouses, and several additional facilities.

Bakker planned to finance these projects by selling lifetime partnerships. He offered eleven different partnership programs ranging in cost from $500 to $10,000. Eight of the partnerships promised benefits that included annual lodging in one of the Heritage Village facilities. In January 1984, [Bakker] began using the mail to solicit lifetime partners. Also, from February 1984 through May 1987, Bakker used broadcasts carried on the PTL Television Network and various commercial affiliates to solicit lifetime partners. Many of these partners drew on meager

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"partnerships" which purported to provide to purchasers the right to varying numbers of nights each year at various PTL hotels at Heritage, USA, the vacation retreat constructed by PTL. We refer to all such offerings collectively as LTPs and to purchasers of LTPs as "lifetime partners" or simply as "partners."

incomes to purchase Heritage Village lodging benefits. [Bakker] raised at least $158 million through the sale of approximately 153,000 partnerships with lodging benefits.

Bakker promised television viewers that he would limit the sale of partnerships to ensure that each partner would be able to use the facilities annually. [Bakker], however, oversold the partnerships. He promised, for instance, to limit the sale of Grand Hotel partnerships to 25,000 but actually sold 66,683. In addition, Bakker used relatively few of the funds solicited from the partners to construct promised facilities. In fact, of the proposed Heritage Village facilities, only the Grand Hotel and one bunkhouse were actually completed. Instead, Bakker used partnership funds to pay operating expenses of the PTL and to support a lavish lifestyle.... This combination of overselling partnerships and diverting partnership proceeds meant that the overwhelming majority of the partners never received the lodging benefits Bakker promised them.

925 F.2d at 731-32 (4th Cir. 1991).[3]

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[3]PTL's desire for unbridled growth is captured in the following passage found in a major PTL publication:

> Enlarge your house; build on additions; spread out your home! For you will soon be bursting at the seams ...

Jim & Tammy Bakker, *Jim & Tammy Bakker Present the Ministries of Heritage Village Church* 198 (1986) (quoting Isaiah *54:2).*

Some additional facts will allow for a more complete understanding of the circumstances involved herein. First, when PTL announced the beginning of the LTP program and the construction of the Heritage Grand Hotel in December of 1983, the program was limited to 25,000 subscribers. As of May 31, 1984, the end of the last fiscal year audited by DH & S, approximately 17,000 LTPs had been purchased. In September of 1984, after [*983*] DH & S had completed its audit field work, a PTL vice-president informed DH & S that construction of a second hotel, the Heritage Towers, was planned and that the LTP program was to be expanded so as to increase the maximum number of potential subscribers by 30,000 to a total of 55,000. Upon learning of PTL's contemplated expansion of the LTP program, DH & S added a note, dated October 24, 1984, to the financial statement it had prepared for PTL's 1984 fiscal year; this note detailed the PTL's planned expansion of the LTP program.

Plaintiffs contend that DH & S was aware of, but failed to disclose, oversales of LTPs. The evidence shows that DH & S checked and knew that, with regard to LTP sales, in April of 1984, "$17,000,000 in pledges has been received of which approximately $9,000,000 has been collected," J.A. 2045, and that, in May of 1984, "$22 million [had been] pledged toward [the] Heritage Grand Hotel," J.A. 1978. By the end of the last fiscal

year for which DH & S performed an audit, then, there were no oversales. The evidence also shows that, by August 25, 1984, prior to the completion of DH & S's field audit, LTP payments had grown to $30.7 million, with an additional $15 million more pledged. J.A. 2567. There is no evidence, however, that DH & S was aware of these oversales at the time.

During the 1980's, the PTL board awarded Bakker, his wife, Tammy Faye Bakker ("Tammy"), and Dortch numerous sizeable bonuses. For example, in 1984 Bakker received $640,000; in 1985 he received $450,000; in 1986 he received $600,000; and in 1987 Bakker was given $1,167,605. J.A. 2366. Bakker's benefits also were tremendous. [4] The compensation, bonuses and cash benefits paid to Bakker, Tammy and Dortch all came from the Executive Payroll Account managed, through mid-1985, by DH & S.

The board overwhelmingly approved the compensation for Bakker, Tammy and Dortch. The only exceptions to unanimous votes were an occasional negative vote or abstention cast by directors who were the direct beneficiaries of the board's action, usually Bakker and Dortch.

Although Cortese was a board member, she had little business experience. As a consequence, when issues

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[4] Bakker's extravagant benefits included the use of a luxury parsonage, complete with an air-conditioned treehouse and personal waterslide.

with respect to which she lacked expertise arose, Cortese consulted with other board members including, in particular, Dortch.

During the same period of time in which Bakker, Tammy, and Dortch were receiving large amounts of money from PTL, PTL's vice-president in charge of finance issued repeated warnings of the economic woes which PTL was barely enduring. A January 1984 memorandum informed Bakker that PTL owed $9.3 million on a past due loan and owed a total of $13 million to all creditors. Bakker was admonished to "[c]urtail as much future spending as possible for the next two months ... [because PTL was] not able to make commitments to anyone else." J.A. 1821. A March 1984 memorandum to Dortch stressed the "need to seriously trim our payroll." J.A. 1823. The memorandum continued: "Each day brings us into a deeper crisis." *Id.* A November 1984 memorandum to Bakker stated: "Until contributions come up to the levels of our current operational expenses, it will continue to be necessary to cover operating expenses from the Tower funds." J.A. 1838. Another memorandum later that month stated succinctly: "We are in a very serious cash flow position." J.A. 1840.

A draft of DH & S's audit report for the fiscal year ending May 31, 1984, expressed concern over "whether PTL w[ould] be able to continue as 'a going concern' based on current assets of only [$]8.6 million against [$]28.5 million in current liabilities." J.A.

2046. Such concern, however, was expurgated from the report before its issuance.

As indicated by the excerpt, quoted above, from a PTL internal memorandum, to help meet the demands for cash which PTL was experiencing, Bakker diverted funds earmarked for the construction of facilities for the Lifetime Partners to various operating [*984*] expenses. Yet, despite the dire financial straits in which PTL found itself and the IRS's decision, in late 1983, to audit PTL, Bakker issued to prospective lifetime partners a brochure promoting the LTPs which stated: "You cannot find a better investment opportunity anywhere...." J.A. 2185E. Bakker made similar representations enticing viewers to purchase LTPs on television.

As mentioned above, in late 1983, PTL fell prey to an IRS audit which culminated in PTL being stripped of its tax-exempt status. The IRS took this action in part due to private inurement allocated to Bakker and Tammy. The loss of tax exempt status threatened to create huge tax liabilities and to leave PTL unable to attract the deductible contributions which were its lifeblood.

A DH & S workpaper prepared in relation to DH & S's 1983 six-month review of PTL states: "IRS exam will find private inurement [and] it'll go to court [and] we'll lose." J.A. 2148. DH & S did, in a note to its 1984 audit report, make reference to the fact that the IRS had commenced its own audit of PTL, although no

specific mention was made of the issue of private inurement.

Plaintiffs focus their attention on DH & S and allege that the accounting firm aided and abetted Bakker's claimed frauds in several ways. First, as noted above, plaintiffs argue that DH & S was, in fact, aware of the oversale of LTPs. Second, plaintiffs claim that DH & S had knowledge that PTL was having difficulties in maintaining its solvency but concealed this problem from the partners under pressure from PTL. Third, plaintiffs further argue that DH & S must have had knowledge of the diversion of hotel construction funds because it prepared PTL's checks to pay construction costs. Fourth, plaintiffs contend that DH & S deliberately concealed the likelihood that the IRS would make a finding of private inurement and, as a consequence, strip PTL of its tax-exempt status. Last, plaintiffs urge that DH & S must have been aware of the exorbitant benefits being awarded to Bakker and Dortch by virtue of its administration of PTL's "Executive Payroll Account," yet failed to make any disclosure.

DH & S and Cortese both contend that Bakker and Dortch actively concealed information from PTL's board regarding possible timeshare or securities violations, private inurement concerns, the instability of PTL's tax exempt status, oversales of partnerships, use of partnership funds to pay Bakker's bonuses, and PTL's path to insolvency.

B.

On November 17, 1987, a class of plaintiffs comprised of approximately 160,000 individuals who had purchased the PTL LTPs filed the instant suit. At trial, plaintiffs pursued claims of common law fraud, fraud in violation of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), fraud in violation of the North Carolina Securities Act, N.C. Gen. Stat. §§ 78A-1 to 78A-65, fraud in violation of the South Carolina Timeshare Act ("SCTSA"), S.C.Code Ann. §§ 27-32-10 to 27-32-250, violations of the federal Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. §§ 1961-1968, and of the North Carolina Racketeer Influenced and Corrupt Organizations Act ("NC-RICO"), N.C.Gen.Stat. §§ 75D-1 to 75D-14, and common law negligence. An extensive jury trial was conducted. Near the close of evidence, the district judge granted a directed verdict on the securities fraud claims on the ground that the LTPs were not "securities." The court then submitted the following issues to the jury: (1) whether Bakker violated federal RICO and NC-RICO; (2) whether Taggart or DH & S aided or abetted Bakker's alleged RICO or NC-RICO violations, or conspired to commit such violations; (3) whether Bakker committed common law fraud, and whether DH & S aided and abetted Bakker's alleged common law fraud or conspired to commit such fraud; (4) whether the partnerships were "timeshares" under the SCTSA and whether Bakker had violated the SCTSA,

and whether DH & S had aided and abetted Bakker's alleged violation of SCTSA or conspired to commit such a violation; and (5) whether Taggart or Cortese were grossly negligent.

The jury returned a verdict against Bakker on the common law fraud count. With this one exception, it refused to place liability [*985*] on any defendants for any of the remaining claims. The district court entered judgment accordingly. Plaintiffs filed a motion for a new trial which was denied. *See* Fed.R.Civ.P. 59. DH & S, Taggart and Cortese each moved to assign costs to plaintiffs pursuant to Federal Rule of Civil Procedure 54(d). Despite the verdict in favor of Taggart and DH & S, the trial judge refused to award attorney's fees to either because he considered it to have been a "relatively close and difficult" case as to their liability. J.A. 1815. He did award Cortese attorney's fees because he found the case brought against her "was neither close nor difficult." J.A. 1816.

Plaintiffs appeal, contending that the motion for a new trial was improperly denied because the verdicts handed down by the jury were "against the clear weight of the evidence," *e.g., Poynter ex rel. Poynter v. Ratcliff*, 874 F.2d 219, 223 (4th Cir.1989), for a wide variety of reasons. They also assert that the district court's jury instructions were riddled with errors requiring reversal. Plaintiffs challenge as well the appropriateness of the district court's grant

of a directed verdict on the securities fraud claims and several evidentiary rulings. Bakker has filed a cross-appeal in which he contends that the district court erred in failing to resolve the issues of reliance, causation and damages on an individual class member basis. Taggart and DH & Shave filed a cross-appeal challenging the denial of their motions for costs against the plaintiff class.

II.

Plaintiffs raise a plethora of assignments of error with respect to the various counts they have brought against the defendants. [5] In order to facilitate our discussion, we briefly summarize the standards of

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[5] We would inform counsel for the plaintiff class that the attempts taken to avoid the page limitation set by Federal Rule of Appellate Procedure 28(g) have not gone unnoticed. After the parties were granted a ten-page extension in the length of the briefs from 50 to 60 pages, counsel attempted to evade the 60 page limitation by improperly spacing words and citations, using footnotes for case cites rather than citing cases in the body of the brief, extending pages, and reducing margins. These tactics make it more difficult for this Court to read the plaintiffs' brief and extract the plaintiffs' arguments. Counsel should remember that "[j]udges are not like pigs, hunting for truffles buried in briefs." *United States v. Dunkel*, 927 F.2d 955, 956 (7th Cir.1991). A client's interests are not furthered by drafting briefs which serve to camouflage legal issues. We would in general admonish all counsel that they, as officers of this Court, have a duty to uphold faithfully the rules of this Court.

review applicable to plaintiffs' assignments of error. We review *de novo* the district court's grant of a motion, pursuant to Federal Rule of Civil Procedure 50, for a directed verdict. *Gairola v. Virginia Dep't of Gen'l Servs.*, 753 F.2d 1281, 1285 (4th Cir.1985). We review the denial of a motion for a new trial pursuant to Federal Rule of Civil Procedure 59 solely for abuse of discretion. *Poynter ex rel. Poynter*, 874 F.2d at 223. In reviewing the adequacy of the district court's choice of jury instructions, we accord the district court much discretion and will not reverse provided that the instructions, taken as a whole, adequately state the controlling law. *Lohrmann v. Pittsburgh Corning Corp.*, 782 F.2d 1156, 1164 (4th Cir.1986).

III.

We consider first the district court's grant of a directed verdict against plaintiffs as to their securities fraud claim. Plaintiffs urge that the LTPs constituted "securities" within the meaning of the securities acts, and that, as a consequence, the use of fraud in the sale of the LTPs contravened Section 10(b) of the federal Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5, as well as the antifraud provision of the North Carolina Securities Act, N.C.Gen.Stat. § 78A-8.

The district court explained its reasons for granting defendants' motion for a directed verdict

thus:

> In *United Housing Foundation v. Forman*, 421 U.S. 837, 95 S.Ct. 2051, 44 L.Ed.2d 621 (1975), the United States Supreme Court held that "when a purchaser is motivated by a desire to use or consume the item purchased ... the securities laws do not apply." *Id.* at 852-53 [95 S.Ct. at 2060-61] (footnote and citation omitted). [*986*] Under *Forman*, the lifetime partnerships at issue in this case are not securities as a matter of law.

J.A. 1799. The district court cited no facts in support of its conclusion.

"Security," for purposes of federal securities regulation, is defined in Section 2(1) of the Securities Act of 1933, 15 U.S.C. § 77b(1), and in Section 3(10) of the Securities Exchange Act of 1934, 15 U.S.C. § 78c(10). [6] Among the several definitions provided in both sections, securities are defined to encompass "investment contracts." Plaintiffs allege that the LTPs constitute "investment contracts."

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[6] These two sections differ only slightly as far as wording and are generally accepted to be indistinguishable. *E.g., Landreth Timber Co. v. Landreth*, 471 U.S. 681, 686 n. 1, 105 S.Ct. 2297, 2301 n. 1, 85 L.Ed.2d 692 (1985). For purposes of this discussion we discuss, without distinguishing, cases addressing the definition of "security" under both acts.

The determination of whether a placement of money constitutes an "investment contract" calls for examining the facts under the test enunciated in *SEC v. W.J. Howey Co.*, 328 U.S. 293, 298-99, 66 S.Ct. 1100, 1103, 90 L.Ed. 1244 (1946). The *Howey* test instructs that an investment contract exists where there has been (i) an investment of money (ii) in a common enterprise (iii) with an expectation of profits garnered "solely" from the efforts of others. [7] At issue here is whether the third prong, that plaintiffs made their investment with an expectation of profits solely from the efforts of others, is met. [8]

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[7] "Despite the restrictive language of the third prong of the test,later courts have explained that a program requiring some effort from the investor may still constitute an 'investment contract,' but the most essential functions or duties must be performed by others and not the investor." *Bailey v. J.W.K. Properties, Inc.*, 904 F.2d 918, 920 (4th Cir.1990).

[8] The parties do not contest that the remaining prongs of the *Howey* test can be met on the record before us. We note, in particular, that, because we find that "profits" under the LTP scheme are distributed *pro rata* to lifetime partners, there is horizontal commonality, *see Revak v. SEC Realty Corp.*, 18 F.3d 81, 87 (2d Cir.1994), in this case. This means that we need not decide here whether some form of vertical commonality, see id. *at 87-88, might satisfy the second prong of the Howey* test.

The fact that there is horizontal commonality here also allows us to distinguish this case from *Revak v. SEC Realty Corp., supra*, and *Wals v. Fox Hills*

The Supreme Court considered *Howey's* third prong in the context of an offering of interests in real estate in *United Housing Foundation v. Forman*, 421 U.S. 837, 95 S.Ct. 2051, 44 L.Ed.2d 621 (1975). There the Court was faced with the question of "whether shares of stock entitling a purchaser to lease an apartment in ... a state subsidized and supervised nonprofit housing cooperative ... are 'securities'." *Id.* at 840, 95 S.Ct. at 2054. The Court answered this question in the negative, explaining:

> The touchstone [of the *Howey* test] is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others. By profits, the Court has meant

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Development Corp., 24 F.3d 1016 (7th Cir.1994), two recent cases where the Second and Seventh Circuits, respectively, found no security arising from the sale of condominium interests because of the absence of commonality. In particular, in *Revak*, there was no rental pool arrangement; that case involved merely the sale of condominiums. For that reason, the Second Circuit found that neither horizontal commonality nor strict vertical commonality, assuming the latter adequate to satisfy *Howey*, was present. Wals *presented the Seventh Circuit with a case in which there were rental pool arrangements. The arrangements, however, were individual contracts between each purchaser and the developer. Because there was no overarching rental pool arrangement according to which profits would be distributed* pro rata *among all purchasers, the Seventh Circuit found that horizontal commonality, which that court reads the Howey* test to require, was not present.

> either capital appreciation resulting from the development of the initial investment ... or a participation in earnings resulting from the use of investors' funds.... In such cases the investor is "attracted solely by the prospects of a return" on his investment. *Howey, supra*, [328 U.S.] at 300 [66 S.Ct. at 1103]. By contrast, when a purchaser is motivated by a desire to use or consume the item purchased--"to occupy the land or to develop it themselves," as the *Howey* Court put it, *ibid.*--the securities laws do not apply.

Id. at 852-53, (citations and footnotes omitted). The Court concluded: "In the present case there can be no doubt that investors were attracted solely by the prospect of acquiring a place to live, and not by financial returns on their investments." *Id.* at 853,. Reasoned the Court:

> Nowhere does the [Investment Bulletin circulated to prospective purchasers] seek to attract investors by the prospect of profits resulting from the efforts of the promoters or third parties. On the contrary, the Bulletin repeatedly emphasizes the "nonprofit" nature of the endeavor. It explains that if rental charges exceed expenses the difference will be returned as a rebate, not invested for profit. It also informs purchasers that they will be unable to resell their apartments at a profit since the apartment must first be

> offered back to [the corporation owning the complex] "at the price ... paid for it." [App. 163a.] In short, neither of the kinds of profits traditionally associated with securities was offered to respondents.

421 U.S. at 854.

Forman, we think, makes clear that, for *Howey*'s third prong to be satisfied, it must be shown (1) that the opportunity provided to offerees tended to induce purchases by emphasizing the possibility of profits, (2) that the profits are offered in the form of capital appreciation or participation in earnings within the meaning of *Howey* and *Forman*, and (3) that the profits offered would be garnered from the efforts of others. We turn, then, to an examination of the facts of this case in light of the third prong of the *Howey* test. [9] We note initially that the third element

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[9] *Forman* does not preclude the possibility that an offering of real estate can, as a matter of law, constitute an offering of a security. *E.g., Hocking v. Dubois*, 885 F.2d 1449 (9th Cir.1989) (en banc), cert. denied, *494 U.S. 1078, 110 S.Ct. 1805, 108 L.Ed.2d 936 (1990)*. *Indeed, "[w]hile it is true that ordinary real estate investments, e.g., the purchase of a dwelling, usually are not securities under either Federal or State law, the facts of each case determine whether or not particular instruments are securities." Kosnoski v. Bruce*, 669 F.2d 944, 946 n. 3 (4th Cir.), *cert. denied*, 459 U.S. 832, 103 S.Ct. 72, 74 L.Ed.2d 71 (1982).

We think that the same can be said of the offering of a

delineated above, that is, that the profits offered are garnered from the efforts of others, is not at issue here, *i.e.*, appellees do not dispute that, if there are profits here within the meaning of *Howey* and *Forman* and if offerees would reasonably have been induced to purchase LTPs based upon promises of profit, *Howey*'s third prong is met. We therefore need only

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timeshare. *See* Thomas Lee Hazen, *Treatise on the Law of Securities Regulation* § 1.5, at 30 (2d ed.1990) ("the currently fashionable marketing of real estate interests through time-share or shared equity programs raises securities law issues because of the possibility of finding an investment contract"); *cf. State v. Shade*, 104 N.M. 710, 726 P.2d 864, 869-71 (Ct.App. 1986) (finding that timeshares can be securities under New Mexico securities law which employs the *Howey* test), *writ quashed sub nom. Vincent v. State*, 104 N.M. 702, 726 P.2d 856 (1986), *overruled on unrelated grounds, State v. Olguin*, --- N.M. ----, 879 P.2d 92 (Ct.App. 1994), *cert. granted*, --- N.M. ----, 879 P.2d 91 (1994). (Our use of the term "timeshares" to describe the LTPs at issue here in no way reflects upon the question of whether they qualify as "vacation time sharing plans" as that term is used in the SCTSA. Indeed, we conclude below that the LTPs are not subject to regulation under the SCTSA. *See post*, at 992-94.)

The district court therefore erred in failing to consider the specific facts presented before granting the appellees' motion for a directed verdict. "An action [under the securities laws] should not be dismissed without an exploration of [the promotional] materials where ... the plaintiffs reasonably allege the existence of investment intent and common enterprise and where nothing in the complaint precludes the finding of a security." *Aldrich v. McCulloch Properties, Inc.*, 627 F.2d 1036, 1040 (10th Cir.1980).

consider the first two elements delineated above.

We first observe that the promotional materials circulated by PTL represented that the value of the privileges lifetime partners would receive far exceeded the $1,000 LTP purchase price. We note, in particular, that letters signed by Bakker, promoting the LTPs, state: "You cannot find a better investment opportunity anywhere--you can actually save thousands of dollars during your lifetime with your one-time investment of $1,000 in the ministry of PTL." J.A. 2178. Further, a brochure designed to promote certain LTPs states:

[*988*] There has never been a better value for your investment in the ministry of PTL. For a one-time gift of $1,000 you will be able to stay free for 4 days and 3 nights, every year, for the rest of your life, in the Heritage Grand Hotel!

Think of the thousands of dollars you will save during your lifetime!

According to the current rate of inflation, if you use your PTL Lifetime Partner membership for 40 years, the gift value of your room at the Heritage Grand Hotel could be worth almost $20,000! You will not be able to find a better investment opportunity anywhere!

J.A. 2185E (footnote omitted[10]). Later in the same

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[10]The footnote further emphasizes the economic aspect of the LTPs, stating:

brochure, it is cautioned: "A maximum of 50% of Heritage Grand Hotel rooms will be available at any given time for Lifetime Partners, allowing for proper hotel maintenance and operations." J.A. 2185H. Other brochures contain similar representations, and Bakker made similar representations on his television program.[11]

These promotional materials can be read to suggest that LTP purchasers would receive an economic benefit in the form of discounted lodging privileges at Heritage USA facilities. It can be concluded, moreover, that PTL could offer this benefit by virtue of its operation, at regular prices, of the facilities not occupied by lifetime partners. This conclusion is

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> Based on estimated room rates and the average rate of inflation, the equivalent costs for a Lifetime Partner who stays in the Heritage Grand Hotel 3 nights, every year, for 40 years, would be approximately $19,500.

J.A. 2185E n.*.

[11] For example, on a January 22, 1986, broadcast, Bakker explained:

> Do you know, when somebody found out I was offering $1,000 for seven days and six nights every year, do you know what they [sic] said? You couldn't rent that suite for $1,000 a night for one night, is what it would rent for in a good hotel. So, that means, it is worth $7,000 or $6,000 just for the first week you stay in it.

Tr. 2814.

supported by the fact that at least 50% of such facilities were reserved for regular patrons in order that "proper hotel maintenance and operations" might be maintained.

Appellees urge that members of the plaintiff class who testified at trial indicated that, despite the foregoing statements in the materials promoting the LTPs, they purchased LTPs with personal use, not profit, as the central motivation. However, even granting appellees' characterization of the testimony of these witnesses, such testimony simply cannot be dispositive in the face of evidence that the promoter of the scheme in question marketed the scheme by emphasizing the potential for profit. Indeed, the Court in *Forman* focused not on the testimony of purchasers of cooperative apartments, but on whether the marketing approach adopted by the sellers was likely to induce purchasers interested in turning a profit.[12] 421 U.S. at [*989*] 853-58, 95 S.Ct.

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[12]It would make little sense for the existence of a "security" to turn solely on whether those who actually invest do so without regard to profit. Such a rule would be highly impractical. Would the existence of a "security" change according to each purchaser? If not, how many, or what percentage of, purchasers would have to have made their investments with an eye toward profits in order for there to be "securities"? Finally, how could the SEC be expected to regulate effectively where the existence of a "security" turns not on how and to whom an investment opportunity is offered, but only on those who ultimately undertake such an investment?

at 2061-63; *see Rice v. Branigar Org., Inc.*, 922 F.2d 788, 790 (11th Cir.1991)[13] ("In addition to

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We note that such a rule seems inconsistent with the Supreme Court's holding in *SEC v. Ralston Purina Co.*, 346 U.S. 119, 73 S.Ct. 981, 97 L.Ed. 1494 (1953). There, the Court was faced with the claim by Ralston Purina Co. that an offering of company stock made to its employees was exempt under what is now Section 4(2) of the Securities Act of 1933, 15 U.S.C. § 77d(2), pursuant to which "transactions by an issuer not involving any public offering" are exempt from regulation. Held the Court: "The focus of inquiry [as to whether an offering is public] should be on the need of the *offerees* for the protections afforded by registration." *Id.* at 127, 73 S.Ct. at 985 (emphasis added). The Court concluded that Ralston Purina Co. could not demonstrate that all the employees to whom it had offered stock had access to enough information about the company that it could be concluded that they were not in need of "the protections afforded by registration." Importantly, the Court did *not* look solely to those employees who, in fact, accepted the offer and purchased stock. This holding seems inconsistent with appellees' position: adoption of a test for the existence of a 'security' which looked only to actual purchasers would seem to undermine the Supreme Court's holding in *Ralston Purina Co.*

[13] Appellees rely heavily upon the Eleventh Circuit's decision in *Rice*. There, Justice Powell, writing for the court, held that sales of lots in a residential housing development were not sales of "securities." Appellees make particular reference to the following statement by the court in *Rice*:

> We believe that people buy houses and lots in a beach-club development primarily to use them, not to derive profits from the entrepreneurial efforts of the developers.... The appellants have not offered any evidence to show that the majority or

looking at the motivations of the purchasers, the Supreme Court also has looked to the emphasis provided in the promotional material to determine whether the sale of something is a sale of 'securities' for the

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> even a fair number of the buyers bought houses or lots as an investment.

922 F.2d at 790-91 (citation omitted). Appellees argue that, here, appellants have similarly failed to provide evidence that any class members purchased LTPs as investments.

Appellees' argument ignores the Eleventh Circuit's observation (one that, as noted in the text, we share) that, "[i]n addition to looking at the motivations of the purchasers, the Supreme Court also has looked to the emphasis provided in the promotional material to determine whether the sale of something is a sale of 'securities' for the purpose of federal securities law." 922 F.2d at 790. On this basis, the Eleventh Circuit relied, in support of its holding that no security was present, upon the fact that, in the case before it,

> the promotional materials published to sell the lots at the Landings do not emphasize the investment value of the lots. Of the several marketing items introduced into evidence, there was only one passing reference to buying the property as an investment. The overall emphasis in the promotional material was clearly placed on enjoying the beauty of the island and the amenities of the club and community.

922 F.2d at 791 (citations omitted). The same cannot be said here. As described above, the promotional materials circulated by PTL cannot be said to have focused their emphasis clearly away from the profit aspects of the LTPs. We conclude that *Rice* is factually distinguishable from the case at bar.

purpose of federal securities law."); *Aldrich v. McCulloch Properties, Inc.*, 627 F.2d 1036, 1039-40 (10th Cir.1980) ("Promotional materials, merchandising approaches, oral assurances and contractual agreements were considered in testing the nature of the product in virtually every relevant investment contract case."). In short, "[i]n the present case," we *can and do doubt* whether "investors were attracted solely by the prospect of acquiring a [hotel room to use], and not by financial returns on their investments." *Forman*, 421 U.S. at 853, 95 S.Ct. at 2061.

We conclude, then, that the promotional materials used to market the LTPs can be seen as emphasizing the profit potential of the LTPs. The materials not only speak generally of the LTPs as "investment[s]," but also offer specific calculations of the true value of the LTPs as compared to their purchase price. The materials also allow the reader to infer that the value of the LTPs was enhanced by virtue of the commercial activities of the PTL facilities in catering to patrons paying full price. Moreover, it is clear and, as noted above, undisputed, that this benefit arises from the managerial efforts of others.

For *Howey*'s third prong to be satisfied, the benefit available to lifetime partners must arise either as capital appreciation or as participation in earnings. We believe that the record before us allows for the conclusion that the benefit in this case arises as capital appreciation. Under the LTP scheme, it

seems that the value of the rights to use the various Heritage, USA, facilities would be enhanced, and therefore capital appreciation might accrue, by virtue of the regular commercial operations of half of all the facilities reserved by regular patrons paying full price for their accommodations.

Appellees argue that the LTPs are nontransferable and that, as a consequence, lifetime partners could never realize any capital appreciation that the LTPs might accrue. On the record before us, however, we cannot conclude that the LTPs are nontransferable. Appellees first note that several class members testified that they were unaware that LTPs could be transferred or believed that they could not be. As discussed below, however, testimony as to the beliefs of actual purchasers, even if accurately characterized, is not dispositive. Appellees further note that several of the LTPs offering brochures explicitly prohibit transfer of LTPs. *See*, [*990*] *e.g.*, J.A. 2185H. Plaintiffs, however, submit evidence indicating the contrary. First, forms, purportedly prepared by PTL, which allow for the transfer of LTP benefits on a yearly basis, J.A. 2626, and a letter from PTL to certain LTP holders indicating that their LTPs were in fact transferable, again on a yearly basis, J.A. 2629. Last, PTL records tabulate the number of LTPs "transferred." *See* J.A. 2562-72. A jury might reasonably conclude that this and other references to the increasing value of the LTPs might

lead partners to infer that they had a right to transfer their LTPs. In short, we cannot say with certainty that a jury would necessarily conclude, on the evidence presented, that the LTPs were not transferable. As a consequence, we cannot rule out the possibility that the LTPs offered purchasers the possibility ofrealizing capital appreciation. *See Forman*, 421 U.S. at 854-55, 95 S.Ct. at 2061-62.

Thus, the LTPs cannot be excluded from securities law coverage as a matter of law. This conclusion is buttressed by a 1973 SEC interpretive release, *Offers and Sales of Condominiums or Units in a Real Estate Development*, Securities Act Release No. 5347, 1 Fed.Sec.L.Rep. (CCH) ¶ 1049 (Jan. 4, 1973) (listed at 17 C.F.R. § 231.5347) (acknowledged by the Supreme Court in *Forman*, 421 U.S. at 853 n.17, 95 S.Ct. at 2061 n. 17). The release describes conditions under which offerings of resort condominiums in conjunction with rental arrangements, pursuant to which the condominiums are to be occupied by the owners for part of the year but rented out most of the year, will constitute an offering of securities. The release, after analyzing relevant precedent, concludes:

> [T]he offering of condominium units in conjunction with any one of the following will cause the offering to be viewed as an offering of securities in the form of investment contracts:
>
> 1. The condominiums, with any rental arrangement or other similar service, are offered and

sold with emphasis on economic benefits to the purchaser to be derived from the managerial efforts of the promoter, or a third party designated or arranged for by the promoter, from rental of the units.

2. The offering of participation in a rental pool arrangement; and
3. The offering of a rental or similar arrangement whereby the purchaser must hold his unit available for rental for any part of the year, must use an exclusive rental agent or is otherwise materially restricted in his occupancy or rental of his unit.

1 Fed.Sec.L.Rep. (CCH) ¶ 1049, at 2072. The release contemplates that it would apply "to offerings of all types of units in real estate developments which have characteristics similar to those described herein." *Id.*, at 2071. The reasoning and conclusions set forth in the SEC release seem applicable to offerings of timeshares. [14] Indeed, one leading securities law treatise concludes that "[e]ssentially the same analysis applicable to resort condominiums should apply to timesharing ... offerings." II Louis Loss & Joel Seligman, *Securities Regulation* 970 (1989).

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[14] Our use of the term 'timeshares' to describe the LTPs has no bearing on our analysis of whether the LTPs are subject to regulation under the SCTSA. *See supra* note 9.

The release's third-numbered paragraph, quoted above, seems applicable in the instant case. The LTPs were offered subject to material restrictions as to partners' rights to occupy the various Heritage, USA resorts. In particular, partners were limited with respect to the amount of time each year that they could make use of the various resorts, and their rights to visit the resorts were conditioned upon the requirement that 50% of the resorts remain available for ordinary patrons who were not LTP holders. In effect, partners were required to hold their "interest" in the resorts available for rent during the majority of the year that they did not make use of the resorts.

Thus, we cannot conclude, on the record before us, that the LTPs are not securities. Such a determination is properly made by a jury. *See Zolfaghari v. Sheikholeslami*, 943 F.2d 451, 456 (4th Cir.1991). We therefore conclude that the district court erred in granting appellees' motion for a directed verdict [*991*] on plaintiffs' federal securities fraud claim against Bakker. We reach a similar conclusion with respect to plaintiffs' state securities fraud claim against Bakker. *See* N.C.Gen.Stat. § 78A-2(11) (defining "[s]ecurity" to include "investment contract").

Despite our conclusion that a jury question exists as to whether the LTPs constituted "securities," however, we must affirm the district court's dismissal of plaintiffs' claim that DH & S aided and abetted

Bakker's alleged federal securities fraud violation. In its recent opinion in *Central Bank of Denver, N. A. v. First Interstate Bank of Denver, N. A.*, --- U.S. ----, 114 S.Ct. 1439, 128 L.Ed.2d 119 (1994), the Supreme Court held that Section 10(b) does not support claims for aiding and abetting. On this basis, then, we affirm the district court's judgment as to this count.

Remaining for our review is the district court's dismissal of plaintiffs' claim that DH & S aided and abetted Bakker's alleged North Carolina violation of N.C.Gen.Stat. 78A-8. In resolving this question of state law such as this, we must, in the absence of definitive authority from North Carolina's highest court, attempt to divine what that court would do were it faced with this question. *See Roe v. Doe*, 28 F.3d 404, 406-07 (4th Cir. 1994). We would note that the Supreme Court of North Carolina has stated, in a case raising the issue of whether the *in pari delicto* defense applied to insider trading actions brought under the North Carolina securities law, that it "pay [s] great deference ... to decisions of the Supreme Court of the United States when they address issues similar to those before us in a given case." *Skinner v. E.F. Hutton & Co.*, 314 N.C. 267, 333 S.E.2d 236, 239 (1985).[15] This suggests that,

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[15]We note, however, that, although the Supreme Court of North Carolina in *Skinner* relied heavily upon the opinion of the United States Supreme Court in

with regard to the issue now under discussion, the Supreme Court of North Carolina would follow the Supreme Court's holding in *Central Bank of Denver, N. A.* and conclude that the North Carolina anti-fraud provision does not support a cause of action for aiding and abetting a substantive violation thereof.

The issue proves more complicated than that, however. Examination of the language and form of the controlling North Carolina statute, N.C. Gen.Stat. § 78A-8, reveals that the statute "closely parallels the S.E.C. Rule 10b-5." [16] *Skinner v. E.F. Hutton*

Bateman Eichler, Hill Richards, Inc. v. Berner, 472 U.S. 299, 105 S.Ct. 2622, 86 L.Ed.2d 215 (1985), and found its "reasoning [to be] compelling," 333 S.E.2d at 239, the state supreme court nevertheless rejected the Court's conclusion that the *in pari delicto* defense might have some role to play in federal securities laws litigation, concluding that the defense was wholly inapplicable to insider trading actions brought under the North Carolina securities law, *id.* at 240.

[16] N.C.Gen.Stat. § 78A-8 provides:

> It is unlawful for any person, in connection with the offer, sale or purchase of any security, directly or indirectly:
>
> (1) To employ any device, scheme, or artifice to defraud,
>
> (2) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or,

& Co., 70 N.C.App. 517, 320 S.E.2d 424, 427 (1984), *aff'd in part and rev'd in part*, 314 N.C. 267, 333 S.E.2d 236 (1985). We must assume that the North Carolina legislature consciously chose to model its anti-fraud provision on an SEC rule and not on the underlying federal statute. This assumption casts doubt upon whether the Supreme Court's holding in *Central Bank of Denver, N.A.*, based as it was upon an interpretation of Section 10(b) and not Rule 10b-5, should dictate that North Carolina law similarly does not recognize a cause of action for aiding and abetting a fraud in violation of state securities law.[17]

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(3) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

[17]The United States Supreme Court has, in many Section 10(b) cases, emphasized that the first resort, in determining the breadth of statutory and regulatory coverage, is to the language of the statute and that, while Rule 10b-5 may, on its face appear to embrace wider coverage than does Section 10(b), the SEC does not have the authority to broaden the coverage of Section 10(b) as enacted by Congress. s.g., Central Bank of Denver, --- U.S. at ----, 114 S.Ct. at 1446; *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 472-74, 97 S.Ct. 1292, 1300-01, 51 L.Ed.2d 480 (1977); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 212-14, 96 S.Ct. 1375, 1390-91, 47 L.Ed.2d 668 (1976). For example, in *Hochfelder*, 425 U.S. at 212, 96 S.Ct. at 1390, the Court observed:

[*992*] We nevertheless find the United States Supreme Court's opinion in *Central Bank of Denver, N. A.* persuasive as to the North Carolina state law question. Included in the opinion, as an independent ground for the Supreme Court's holding, is the following:

> Our reasoning is confirmed by the fact that respondents' argument would impose 10b-5 aiding and

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> The [SEC] contends ... that subsections (b) and (c) of Rule 10b-5 are cast in language which--if standing alone--could encompass both intentional and negligent behavior.... Viewed in isolation the language of subsection (b), and arguably that of subsection (c), could be read as proscribing, respectively, any type of material misstatement or omission, and any course of conduct, that has the effect of defrauding investors, whether the wrongdoing was intentional or not.

The Court concluded, however, that what Rule 10b-5 might mean if "[v]iewed in isolation" was irrelevant: at all events, the SEC could not, by regulation, broaden the statutory scope of Section 10(b), and the liability imposed by Section 10(b), the Court found, did not extend to negligent conduct, 425 U.S. at 214, 96 S.Ct. at 1391.

We, of course, need not determine here whether Section 78A-8 extends to negligent conduct. We do, however, observe that such a determination is unclear in light of the similarity of Section 78A-8 to Rule 10b-5 and that, similarly, the determination of whether other issues resolved under Section 10(b) and Rule 10b-5, such as the determination of whether a private cause of action for aiding and abetting liability exists, would apply analogously to North Carolina securities law is unclear.

> abetting liability when at least one element critical for recovery under 10b-5 is absent: reliance. A plaintiff must show reliance on the defendant's misstatement or omission to recover under 10b5. *Basic Inc. v. Levinson*, [485 U.S. 224, 243, 108 S.Ct. 978, 989, 99 L.Ed.2d 194 (1988)]. Were we to allow the aiding and abetting action proposed in this case, the defendant could be liable without any showing that the plaintiff relied upon the aider and abettor's statements or actions. See also [*Chiarella v. United States*, 445 U.S. 222, 228, 100 S.Ct. 1108, 1115, 63 L.Ed.2d 348 (1980)] (omission actionable only where duty to disclose arises from specific relationship between two parties). Allowing plaintiffs to circumvent the reliance requirement would disregard the careful limits on 10b-5 recovery mandated by our earlier cases.

--- U.S. at ---- - ----, 114 S.Ct. at 1449-50. Under the North Carolina Supreme Court's opinion in *Skinner*, this reasoning, grounded upon Rule 10b-5, is equally applicable to plaintiffs' claim against DH & S brought under Section 78A-8.[18]

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[18] The opinion of the North Carolina Court of Appeals in *State v. Williams*, 98 N.C.App. 274, 390 S.E.2d 746, 750 (1990), where the court reviewed the criminal conviction of an attorney for violating N.C.Gen.Stat. § 78A-8, provides additional support for this conclusion. There, although the question of criminal

In summary, we reinstate plaintiffs' securities fraud claims under federal and state law against Bakker, but we affirm the dismissal of plaintiffs' federal and state securities fraud claims against DH & S.

IV.

The jury rejected plaintiffs' claim of timeshare fraud under the SCTSA. The district court denied plaintiffs' motion for a new trial, from which denial plaintiffs appeal. Because we conclude that the LTPs at issue in this case are not "vacation time sharing plan[s]" subject to regulation under the SCTSA, we affirm the district court's denial of plaintiffs' motion in this regard.

The SCTSA proscribes fraud in connection with the sale of "vacation time sharing plans." S.C.Code Ann. § 27-32-110; *see generally* Michelle D. Brodie, Note, *Regulation of Time Sharing in South Carolina*, 37 S.C. L.Rev. 527 (1986). The phrase "vacation time

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aiding and abetting liability under North Carolina securities law was not squarely raised, *compare Central Bank of Denver*, --- U.S. at ----, 114 S.Ct. at 1455 (noting that "an aider and abettor of a criminal violation of any provision of the 1934 Act, including § 10(b), violates 18 U.S.C. § 2"), the state appellate court in Williams *strictly construed criminal liability under the state securities law. We believe that North Carolina courts would not construe the analogous civil liability significantly more broadly in this respect.*

sharing plan" is elucidated by statutory definitional provisions. First, " '[v]acation time sharing plan' means either a vacation time sharing ownership plan or a vacation time sharing lease plan." S.C.Code Ann. § 27-32-10(10). Pertinent here,

> [*993*] "[v]acation time sharing lease plan" means any arrangement, plan or similar devise, whether by membership agreement, lease, rental agreement, license, use agreement, security or other means, whereby the purchaser receives a right to use accommodations or facilities, or both, but does not receive an undivided fee simple interest in the property, for a specific period of time during any given year, but not necessarily for consecutive years, *and which extends for a period of more than one year*....

Id. § 27-32-10(9) (emphasis added).[19]

We believe it crucial that the definition of "vacation time sharing lease plan" is restricted to those plans "which extend[ ] for a period of more than one year." This represents a conscious choice by South Carolina's legislature not to regulate, at least under the SCTSA, those timeshare plans which are of less than

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[19] Section 27-32-10(8) provides for an analogous definition for "vacation time sharing ownership plan" which requires that owners receive an undivided ownership interest in, as well as the right to use, the accommodations and/or facility in question.

one year's duration.

The LTPs at issue in this case, by contrast, are the timeshare counterparts of life estates. *See* Brodie, *supra*, at 530-38 (describing the SCTSA as distinguishing between timeshare interests based upon their categorization in terms of traditional fee and nonfee interests in real property). A life estate, of course, may well extend beyond one year's duration. Importantly, however, a life estate may also terminate within one year of its creation. We believe that, just as a contract which persists for the duration of a person's life consequently does not satisfy the Statute of Frauds' requirement that all contracts not to be performed within one year of the contract's making be in writing, *see* S.C.Code Ann. § 32-3-10(5) (requiring that any "action ... brought ... [t]o charge any person upon any agreement that is not to be performed within the space of one year from the making thereof" be in writing),[20] a life estate

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[20]We do not mean for our citation to S.C.Code Ann. § 32-3-10(5) to imply that that provision of that statute of frauds would apply to contracts regarding timeshare purchases. *See* S.C.Code Ann. § 32-3-10(4) (requiring that "any action ... brought ... [t]o charge any person upon any contract or sale of lands, tenements or hereditaments or any interest in or concerning them" be in writing); *id.* § 27-35-20 (requiring that "[a]ny agreement for the use or occupation of real estate for more than one year" be in writing); *Player v. Chandler*, 299 S.C. 101, 382 S.E.2d 891, 894 (1989) (suggesting that, in an action brought by lessees against lessors regarding

timeshare interest cannot satisfy the statutory requirement that the timeshare plan "extend[ ] for a period of more than one year." The state legislature has not chosen to extend timeshare fraud protection beyond terms of years to life estates, and it is not for us to second-guess that choice.

We conclude that the LTPs sold by PTL are not "vacation time sharing plans" as a matter of law and, on that basis, affirm the judgment entered against the plaintiff class on their timeshare fraud claims.[21]

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oral modifications of a written lease contract, S.C.Code Ann. §§ 32-3-10(4), 32-3-10(5), and 27-35-20 might all have applicability). We wish only to note that the concept that a contract that lasts only for a person's life is not considered to be a contract that necessarily extends for any length of time is quite common in our law and that, therefore, it is not unreasonable to expect that, had South Carolina's legislature intended to regulate timeshares that are keyed to the holder's life, it would have made that intention explicit in the statute.

[21] We feel compelled to note a grave error on the part of the trial court. The district court allowed into evidence the testimony of two "expert witnesses" called by DH & S: David Martin, who, while serving as general counsel to the South Carolina Real Estate Commission, drafted the SCTSA; and Aleta Pillick, an attorney who, while in her former employ with the South Carolina Tax Commission, investigated the LTPs and concluded that they were not timeshares. By admitting this evidence, the district court treated the proper interpretation of the relevant statutory provision, S.C.Code Ann. § 27-32-10(9), as a matter properly resolved by the jury. As we make clear in the text, this question is purely one of law and is

[*994*] V.

Plaintiffs allege that the district court erred in denying their motion for a new trial with respect to their claim against DH & S for aiding and abetting, and conspiring in, Bakker's common law fraud. We conclude, however, that the district court did not abuse its discretion in denying this motion. While the record contains evidence which supports plaintiffs' various theories of aiding and abetting liability on the part of DH & S, we cannot say that the district court abused its discretion in concluding that the jury's verdict was neither against the clear weight of the evidence nor manifestly unjust. *See Poynter ex rel. Poynter,*

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properly resolved by the court; indeed, the proper resolution of this question mandates judgment for appellees, leaving nothing for the jury to determine. Moreover, even were there a material question of fact relating to the duration of the LTPs, it would still be error for the district court to have allowed the testimony of the witnesses listed above into evidence. Expert testimony as to the proper interpretation of applicable domestic law is inadmissible. *Adalman v. Baker, Watts & Co.*, 807 F.2d 359, 366-67 (4th Cir.1986). "[I]t is the responsibility--and the duty--of the court to state to the jury the meaning and applicability of appropriate law, leaving to the jury the task of determining the facts which may or may not bring the challenged conduct within the scope of the court's instruction as to the law." *Id.* at 366. *See* Fed.R.Evid. 702 (expert testimony is admissible to the extent that it "will assist the trier of fact to understand the evidence or to determine a fact *in issue" (emphasis added)).*

supra, 874 F.2d at 223. Appellants, in effect, ask us to retry issues already heard and ruled upon by a jury. This we will not do. It is indeed a rare case where we will second-guess both the jury and the district court in this regard. Nothing in the case now before us warrants such action here.[22]

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[22] Plaintiffs raise, in addition, two legal arguments with regard to the district court's handling of their common law fraud claim against DH & S. They first argue that the district court's jury instruction misled thejury with respect to the applicable statute of limitation. North Carolina law requires that an action for fraud be brought within three years of the accrual of the cause of action; "the cause of action shall not be deemed to have accrued until the discovery by the aggrieved party of the facts constituting the fraud." N.C.Gen.Stat. § 1-52(9). Plaintiffs argue that the district court's jury instruction left the jury with the impression that the three-year statute of limitation ran, without qualification, from the date the fraud was perpetrated and not from the date the fraud was, or should reasonably have been, discovered. The record refutes this argument, however. The jury instruction, as a whole, adequately elucidated the relevant law. Thus, although the statute of limitations instruction need not have been delivered as it appears that no Lifetime Partners were aware of PTL's financial difficulties until 1986, the delivery of the instruction led to no prejudicial error.

Plaintiffs also allege that the district court erred in prohibiting counsel for plaintiffs from making reference to DH & S's failure to call a witness who, plaintiffs claim, would have substantiated their fraud claims against DH & S. In order for it to be appropriate for the jury to draw an adverse inference from the failure of a party to call a witness, the witness must not be "equally available to either

VI.

We turn next to the plaintiff class's RICO and NC-RICO claims. The jury heard the evidence presented and ruled against the class on each of these claims. The district court denied plaintiffs' motion for a new trial, from which denial they now appeal.

As stated above, we review the district court's denial of a motion for a new trial solely for abuse of discretion. We have little trouble concluding that the district court was well within its authority in ruling as it did in the case at bar.[23]

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party." *Dunlap v. G. & C. Towing, Inc.*, 613 F.2d 493, 497 (4th Cir.1980). In *Dunlap*, we noted that plaintiff's treating physician was, in fact, "equally available to either party." *Id.* Here, Fisher, a former employee of DH & S, was, at the time of trial, no longer in DH & S's employ. We see no reason why Fisher was not equally available to be called by plaintiffs as by DH & S and, consequently, find no error in the district court's action.

[23]Plaintiffs also raise two matters of law with respect to the RICO and NC-RICO verdicts. Plaintiffs first submit that the district court erred in leaving it to the jury to determine whether Bakker committed the requisite RICO predicate acts. They argue that, in light of Bakker's previous convictions, affirmed by this Court, for mail and wire fraud, that element of RICO and NC-RICO was established by collateral estoppel. Plaintiffs failed to raise this argument to the district court, whether in the form of a motion for partial summary judgment, suggested jury instructions or otherwise. Given plaintiffs' failure to raise the issue of collateral estoppel to the court below, we decline to consider the argument here. *See Liberty Corp. v. NCNB Nat'l Bank*

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of South Carolina, 984 F.2d 1383, 1389-90 (4th Cir.1993).

Plaintiffs next argue that the jury instructions delivered by the district court were erroneous in three respects. They first argue that error arose because the instructions referred to RICO predicate acts as "crimes." At no time, however, did the district court instruct the jury that RICO required proof of a predicate act beyond a reasonable doubt. Review of the record, however, convinces us that the RICO jury instructions, taken as a whole, fairly state the applicable law in this regard.

Second, with respect to the court's NC-RICO instructions, the district court instructed the jury that proof beyond a reasonable doubt was required under NC-RICO. Plaintiffs agreed below that proof beyond a reasonable doubt was required with respect to Bakker's primary NC-RICO violation but argue that the district court erred in instructing the jury to apply that standard to DH & S's alleged action aiding and abetting Bakker's primary violation. Because the jury found that Bakker had not committed a primary violation, any error in this regard is harmless. We would further note that the fact that the district court emphasized to the jury that it should apply the reasonable doubt standard under NC-RICO supports our conclusion that the jury did not, due to a misunderstanding of the court's instructions, apply the reasonable doubt standard to plaintiffs' RICO claims.

Last, plaintiffs argue that the district court misinstructed the jury as to 18 U.S.C. § 1962(b), which provides:

> It shall be unlawful for any person through a pattern of racketeering activity or through collection of an unlawful debt to acquire or maintain, directly or indirectly, any interest in or control of any enterprise which is engaged in, or the activities of which affect, interstate or

[*995*] VII.

The plaintiff class objects to the district court's instruction to the jury that, in order to find Taggart and Cortese liable, it had to find that they had acted with gross negligence. Plaintiffs claim that, under North Carolina law, directors of a corporation are liable to persons who deal with that corporation for ordinary negligence where such negligence contributes to losses.

We disagree. In *Myers & Chapman, Inc. v. Thomas G. Evans, Inc.*, 323 N.C. 559, 374 S.E.2d 385, 394 (1988), the Supreme Court of North Carolina held that a portion of a trial court's jury instruction

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foreign commerce.

Plaintiffs argue that Section 1962(b) does not require direct equity ownership in the RICO enterprise as plaintiffs contend is required by the court's instruction to the jury that "[a]cquiring an interest in an enterprise means acquiring of [sic] stock or ownership equity, and not merely the existence of an employment relationship with the enterprise." Tr. 8083-84. Further along in the instruction, however, the court instructed: "In order for you to find that plaintiffs have established [that Bakker acquired or maintained an interest in PTL], you must find that Bakker .... gained actual day-to-day involvement in the management and operation of PTL." Tr. 8086. We believe that this explanation sufficiently removed any thought the jury might have had that, to find that Bakker acquired an interest in PTL, it had to find that Bakker acquired an equity interest in PTL. We therefore reject plaintiffs' argument. An analogous argument under NC-RICO similarly fails.

> was erroneous because it suggested to the jury that directors and managing officers are chargeable with an omniscient knowledge of the company's affairs and are liable for damages to third parties resulting from simple negligence. This is not the law in North Carolina. *See Minnis v. Sharpe*, [202 N.C. 300, 162 S.E. 606, *rev'd on other grounds*, 203 N.C. 110, 164 S.E. 625 (1932)].

While plaintiffs attempt to distinguish *Myers & Chapman, Inc.* from the case at bar, we think the holding of that case clearly controls here and reject plaintiffs' attempt to avoid its impact. We therefore find no error in the district court's jury instruction. We also reject plaintiffs' contention that the district court abused its discretion in denying their motion for a new trial on these counts.

VIII.

Bakker cross-appeals from the district court's entry of judgment against him on the common law fraud claim, arguing that the district court erred in not resolving the issues of reliance, causation and damages on an individual and not a classwide basis.[24] Given the facts and circumstances surrounding the LTP scheme and the means according to which the fraud found

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[24]We note, however, that "Bakker does not contest the certification of the class." Appellees' Br. 58.

by the jury was perpetrated, we reject Bakker's contention.

IX.

Taggart and DH & S appeal the denial by the district court of their motion for a grant of costs against the plaintiff class. Prevailing parties are entitled to move for an award of costs pursuant to Federal Rule of Civil Procedure 54(d)(1), [25] which provides, in [*996*] pertinent part: "Except when express provision therefor is made either in a statute of the United States or in these rules, costs ... shall be allowed as of course to the prevailing party unless the court otherwise directs...." The rule makes clear that, in the ordinary course, a prevailing party is entitled to an award of costs. *Constantino v. American S/T Achilles*, 580 F.2d 121, 123 (4th Cir.1978). Indeed, the rule gives rise to a presumption in favor of an award of costs to the prevailing party. *Delta Air Lines, Inc. v. August*, 450 U.S. 346, 352, 101 S.Ct. 1146, 1150, 67 L.Ed.2d 287 (1981); *Coyne-Delany Co. v. Capital Dev. Bd. of Illinois*, 717 F.2d 385, 390 (7th Cir.1983). We have stated that, in a case where the district court feels

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[25] Taggert's and DH & S's motion was, in fact, made pursuant to former Rule 54(d), which, following 1993 amendment of the rule, is now contained, without substantive change except for an express provision that motions for attorney's fees are not meant to be addressed therein, in Rule 54(d)(1).

that aberration from this general rule is appropriate, the court must justify its decision by "articulating some good reason for doing so." *Oak Hall Cap and Gown Co. v. Old Dominion Freight Line, Inc.*, 899 F.2d 291, 296 (4th Cir.1990); *see Constantino*, 580 F.2d at 123 (reversing the district court's denial of costs where the court stated no reason for its action).

We have yet to have occasion to elucidate what might constitute a "good reason" in this context. We look for guidance to the statements of our sister circuits on the matter. The Sixth Circuit has suggested that "good reasons" might include the excessiveness of costs in a particular case, actions taken by the prevailing party which unnecessarily prolonged trial or injected meritless issues, the fact that the prevailing party's recovery is so small that the prevailing party is victorious in name only, and the fact that the case in question was a close and difficult one. *White & White, Inc. v. American Hosp. Supply Corp.*, 786 F.2d 728, 730 (6th Cir.1986). The Seventh Circuit has suggested that "good reasons" may arise from "objective factors [,] such as the resources of the parties, the defendant's efforts or lack thereof to mitigate his damages, and the outcome of the underlying suit." *Coyne-Delany Co.*, 717 F.2d at 392. [26] The Seventh Circuit has also posited

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[26] ***But see Congregation of the Passion, Holy Cross Province v. Touche, Ross & Co.***, 854 F.2d 219, 222 (7th Cir.1988)

that the mere fact that a suit may have been brought in good faith is alone insufficient to warrant a denial of costs in favor of a prevailing defendant. *Id.* We agree; to hold otherwise would frustrate the rule that, in the ordinary case, a prevailing party is entitled to an award of costs, *see id.* This, of course, does not mean that good faith is not a valid factor to consider in determining whether an award of costs is appropriate; to the contrary, it seems to us that good faith on the part of a losing party would be a virtual prerequisite to a denial of costs in favor of the prevailing party.

With this background, we turn to the instant case. The district court found that plaintiffs had rebutted the presumption in favor of awarding Taggart and DH & S their costs on the grounds that plaintiffs had proceeded in good faith, that plaintiffs' case against Taggart and DH & S "was, for the most part, a relatively close and difficult case," J.A. 1815, and on the ground that, given that plaintiffs were in general of modest means and had fallen victim to Bakker's fraud, "it would be inequitable to tax the plaintiffs with the costs incurred by defendants [DH & S] and

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("Generally, only misconduct by the prevailing party worthy of a penalty or the losing party's inability to pay will suffice to justify denying costs."); *Schwarz v. Folloder*, 767 F.2d 125, 131 (5th Cir.1985) (describing the denial of costs as in the nature of a penalty); *Serna v. Manzano*, 616 F.2d 1165, 1167 (10th Cir.1980) (same).

Taggart," *id.*

We review for abuse of discretion the district court's disposition of a victorious party's motion for costs. *Oak Hall Cap and Gown Co.*, 899 F.2d at 296.[27] We cannot say [*997*] that the district court abused its discretion in considering plaintiffs' good faith in pursuing claims against Taggart and DH & S, the closeness of the outcome, or the equities in conducting its analysis; nor do we find any abuse in the district court's conclusion.[28] We consequently reject Taggart's and DH & S's cross-appeals.

CONCLUSION

We find no merit in plaintiffs' remaining assignments of error.[29] We reverse the district

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[27]The Seventh Circuit has suggested that the "abuse of discretion" standard in reviewing Rule 54(d) motions "merges into the standard of simple error used in reviewing decisions of questions of law." *Coyne-Delany Co.*, 717 F.2d at 392. We would simply note that our precedent endorses, without question, the abuse of discretion standard.

[28]We recognize that the district court awarded costs to Cortese and that the only apparent difference between plaintiffs' case against her and their cases against DH & S and Taggert is that the district court felt that the case against Cortese "was neither close nor difficult." J.A. 1816. The district court did not abuse its discretion in determining that, in this case, that factor tipped the scales as to the fortunes of the various parties in this regard.

[29]We note that plaintiffs claim prejudicial error arising from the district court's decision

court's entry of judgment as a matter of law against plaintiffs on their securities fraud claims against Bakker and remand for further proceedings not inconsistent with this opinion. We otherwise affirm the judgments of the district court in all respects.

AFFIRMED IN PART AND
REVERSED AND REMANDED IN PART.

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not to allow plaintiffs to call an expert securities witness because of plaintiffs' tardiness in naming the expert. Given our disposition of plaintiffs' securities fraud claims, we see no reason to address this contention.

FOURTH CIRCUIT DENIAL OF REHEARING

U.S. COURT OF APPEALS FOR THE FOURTH CIRCUIT

NO. 91-2101, -2120, -2121

[STYLE OMITTED]

(Filed: October 18, 1994)

The appellants' petition for rehearing and suggestion for rehearing in banc were submitted to this Court. As no member of this Court or the panel requested a poll on the suggestion for rehearing in banc, and

As the panel considered the petition for rehearing and is of the opinion that it should be denied,

IT IS ORDERED that the petition for rehearing and suggestion for rehearing in banc are denied.

For the Court,

/s/ Bert M. Montague

CLERK

A-52

DISTRICT COURT OPINION

U.S. DISTRICT COURT FOR THE
WESTERN DISTRICT OF NORTH CAROLINA
NO. C-C-87-514-M
[STYLE OMITTED]
(Filed: December 5, 1990)

In United Housing Foundation v. Forman, 421 U.S. 837 (1975), the United States Supreme Court held that "when a purchaser is motivated by a desire to use or consume the item purchased . . . the securities laws do not apply." Id. at 852-53 (footnote and citation omitted). Under Forman, the lifetime partnerships at issue in this case are not securities as a matter of law.

Accordingly, plaintiffs' federal and state securities fraud claims are hereby DISMISSED.

This 5 day of December, 1990.

/s/ James B. McMillan
James B. McMillan
United States District Judge

STATUTES

Securities Exchange Act § 10(b), 15 U.S.C. § 78:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange--

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the [SEC] may prescribe.

SEC Rule 10b-5, 17 C.F.R. § 240.10b-5:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(a) to employ any device, scheme, or artifice to defraud,

(b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) to engage in any act, practice, or course of

business which operates or would operate as a fraud or deceit upon any person.

Federal RICO:

18 U.S.C. § 1961. Definitions

As used in this chapter-

(1) "racketeering activity" means (A) any act or threat involving murder, kidnapping, gambling, arson, robbery, bribery, extortion, dealing in obscene matter, or dealing in narcotic or other dangerous drugs, which is chargeable under State law and punishable by imprisonment for more than one year; (B) any act which is indictable under any of the following provisions of title 18, United States Code: Section 201 (relating to bribery), section 224 (relating to sports bribery), sections 471, 472, and 473 (relating to counterfeiting), section 659 (relating to theft from interstate shipment) if the act indictable under section 659 is felonious, section 664 (relating to embezzlement from pension and welfare funds), sections 891-894 (relating to extortionate credit transactions), section 1029 (relative to fraud and related activity in connection with access devices), section 1084 (relating to the transmission of gambling information), section 1341 (relating to mail fraud), section 1343 (relating to wire fraud), section 1344 (relating to financial institution fraud), sections 1461-1465 (relating to obscene matter), section 1503 (relating to obstruction

of justice), section 1510 (relating to obstruction of criminal investigations), section 1511 (relating to the obstruction of State or local law enforcement), section 1512 (relating to tampering with a witness, victim, or an informant), section 1513 (relating to retaliating against a witness, victim, or an informant, section 1951 (relating to interference with commerce, robbery, or extortion), section 1952 (relating to racketeering), section 1953 (relating to interstate transportation of wagering paraphernalia), section 1954 (relation to unlawful welfare fund payments), section 1955 (relating to the prohibition of illegal gambling businesses), section 1956 (relating to the laundering of monetary instruments), section 1957 (relating to engaging in monetary transactions in property derived from specified unlawful activity), section 1958 (relating to use of interstate commerce facilities in the commission of murder-for-hire), sections 2251-2252 (relating to sexual exploitation of children), sections 2312 and 2313 (relating to interstate transportation of stolen motor vehicles), sections 2314 and 2315 (relating to interstate transportation of stolen property), section 2321 (relating to trafficking in certain motor vehicles or motor vehicle parts), sections 2341-2346 (relating to trafficking in contraband cigarettes), sections 2421-24 (relating to white slave traffic), (C) any act which is indictable under title 29, United States Code, section 186 (dealing with restrictions on payments and loans to labor organizations), or section 501(c)

(relating to embezzlement from union funds,), (D) any offense involving fraud connected with a case under title 11, fraud in the sale of securities, or the felonious manufacture, importation, receiving, concealment, buying, selling, or otherwise dealing in narcotic or other dangerous drugs, punishable under any law of the United States, or (E) any act which is indictable under the Currency and Foreign Transactions Reporting Act;

* * * *

(3) "person" includes any individual or entity capable of holding a legal or beneficial interest in property;

(4) "enterprise" includes any individual, partnership, corporation, association, or other legal entity, and any union or group of individuals associated in fact although not a legal entity;

(5) "pattern of racketeering activity" requires at least two acts of racketeering activity, one of which occurred after the effective date of this chapter and the last of which occurred within ten years (excluding any period of imprisonment) after the commission of a prior act of racketeering activity;

* * * *

18 U.S.C. § 1962. Prohibited activities

(a) It shall be unlawful for any person who has received any income derived, directly or indirectly, from a pattern of racketeering activity or through collection of an unlawful debt in which such person has

participated as a principal within the meaning of section 2, title 18, United States Code, to use or invest, directly or indirectly, any part of such income, or the proceeds of such income, in acquisition of any interest in, or the establishment or operation of, any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce. A purchase of securities on the open market for purposes of investment, and without the intention of controlling or participating in the control of the issuer, or of assisting another to do so, shall not be unlawful under this subsection if the securities of the issuer held by the purchaser, the members of his immediate family, and his or their accomplices in any pattern or racketeering activity or the collection of an unlawful debt after such purchase do not amount in the aggregate to one percent of the outstanding securities of any one class, and do not confer, either in law or in fact, the power to elect one or more directors of the issuer.

(b) It shall be unlawful for any person through a pattern of racketeering activity or through collection of an unlawful debt to acquire or maintain, directly or indirectly, any interest in or control of any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce.

(c) It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign

commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt.

(d) It shall be unlawful for any person to conspire to violate any of the provision of subsections[1] (a), (b), or (c) or this section.

18 U.S.C. § 1964. Civil remedies

(c) Any person injured in his business or property by reason of a violation of section 1962 of this chapter may sue therfor in any appropriate United States district court and shall recover threefold the damages he sustains and the cost of the suit, including a reasonable attorney's fee.

North Carolina Securities Law:

N.C.G.S. § 78A-8

It is unlawful for any person, in connection with the offer, sale or purchase of any security, directly or indirectly:

(1) To employ any device, scheme, or artifice to defraud.

(2) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or,

(3) To engage in any act, practice, or course of business which operates or would operate as a fraud or

deceit upon any person.

North Carolina RICO:

N.C.G.S. § 75D-2. Findings and intent of General Assembly.

(a) The General Assembly finds that a severe problem is posed in this State by the increasing organization among certain unlawful elements and the increasing extent to which organized unlawful activities and funds acquired as a result of organized unlawful activity are being directed to and against the legitimate economy of the State.

(b) The General Assembly declares that the purpose and intent of this Chapter is: to deter organized unlawful activity by imposing civil equitable sanctions against this subversion of the economy by organized unlawful elements; to prevent the unjust enrichment of those engaged in organized unlawful activity; to restore the general economy of the State all of the proceeds, money, profits, and property, both real and personal of every kind and description which is owned, used or acquired through organized unlawful activity by any person or association of persons whether natural, incorporated or unincorporated in this State; and to provide compensation to private persons injured by organized unlawful activity. It is not the intent of the General Assembly to in any way interfere with the attorney-client relationship.

* * * *

N.C.G.S. § 75D-3. Definitions.

As used in this Chapter, the term:

(a) "Enterprise" means any person, sole proprietorship, partnership, corporation, business trust, union chartered under the laws of this State, or other legal entity; or any unchartered union, association, or group of individuals associated in fact although not a legal entity; or any uncharted union, association, or group of individuals associated in fact although not a legal entity; and it includes illicit as well as licit enterprises and governmental as well as other entities.

(b) "Pattern of racketeering activity" means engaging in at least two incidents of racketeering activity that have the same or similar purposes, results, accomplices, victims, or methods of commission or otherwise are interrelated by distinguishing characteristics and are not isolated and unrelated incidents, provided at least one of such incidents occurred after October 1, 1986, and that at least one other of such incidents occurred within a four-year period of the time of the other, excluding any periods of imprisonment, after the commission of a prior incident of racketeering activity.

(c)

(1) "Racketeering activity" means to commit, to attempt to commit, or to solicit, coerce, or intimidate another person to commit an act or acts which would be

chargeable by indictment of such act or acts were accompanied by the necessary mens rea or criminal intent under the following laws of this State.

a. Article 5 of Chapter 90 of the General Statute of North Carolina relating to controlled substances and counterfeit controlled substances

b. Chapter 14 of the General Statutes of North Carolina except Articles 9, 22A, 38, 40, 43, 46, 47, 59 thereof; and further excepting G.S. Sections 14-78.1, 14-82, 14-86, 14-145, 14-146, 14-147, 14-177, 14-178, 14-179, 14-183, 14-184, 14-186, 14-190.9, 14-195, 14-197, 14-201, 14-202, 14-247, 14-248, 14-313 thereof.

c. Any conduct involved in a "money laundering" activity; and

(2) "Racketeering activity" also includes the description in Title 18, United States Code Section 1961(1).

* * * *

N.C.G.S. § 75D-4. Prohibited activities.

(a) No person shall:

(1) engage in a pattern of racketeering activity or, through a pattern of racketeering activities or through proceeds derived therefrom, acquire or maintain, directly or indirectly, any interest in or control of any enterprise, real property, or personal property of any nature, including money; or

(2) conduct or participate in, directly or indirectly, any enterprise through a pattern of racketeering activity whether indirectly, or employed

by or associated with such enterprise; or

(3) conspire with another or attempt to violate any of the provisions of subdivision (1) or (2) of this subsection.

(b) Violation of this section is inequitable and constitutes a civil offense only and is not a crime, therefore an mens rea or criminal intent is not an essential element of any of civil offenses set forth in this section. (1985) (Reg. Sess., 1986), c. 999, s. 1.)

N.C.G.S. § 75D-8. Available RICO civil remedies.

* * * *

(c) Any innocent person who is injured or damaged in his business or property by reason of any violation of G.S. 75D-4 involving a pattern of racketeering activity shall have a cause of action for three times the actual damages sustained and reasonable attorneys fees. For purposes of this subsection, "pattern of racketeering activity" shall require that at least one act of racketeering activity be an act of racketeering activity other than (i) an act indictable under 18 U.S.C. § 1343, or (ii) an act which is an offense involving fraud in the sale of securities. * * * *

(e) A final conviction in any criminal proceeding for a violation of those laws set forth in G.S. 75D-3(c), shall estop the defendant in any subsequent civil action or proceeding under this Chapter as to all matters proved in the criminal proceeding. * * * *

N.C.G.S. § 14-90. Embezzlement of property

received by virtue
of office or employment.

If any person exercising a public trust or holding a public office, or any guardian, administrator, executor, trustee, or any receiver, or any other fiduciary, or any officer or agent of a corporation, or any agent, consignee, clerk, bailee or servant, except person under the age of 16 years, of any person, shall embezzle or fraudulently or knowingly and willfully misapply or convert to his own use, or shall take, make away with or secrete, with intent to embezzle or fraudulently or knowingly and willfully misapply or convert to his own use any money, goods or other chattels, bank note, check or order for the payment of money issued by or drawn on any bank or other corporation, or any treasury warrant, treasury note, bond or obligation for the payment of money issued by the United States or by any state, or any other valuable security whatsoever belonging to any other person or corporation, unincorporated association or organization which shall have come into his possession or under his care, he shall be punished as a Class H felon.

South Carolina Timeshare Law:

S.C. Code 27-32-10 Definitions.

* * * *

(9) "Vacation time sharing lease plan" means any

arrangement plan or similar devise, whether by membership agreement, lease, rental agreement, license, use agreement, security or other means, whereby the purchaser receives a right to use accommodations or facilities, or both, but does not receive an undivided fee simple interest in the property, for a specific period of time during any given year, but not necessarily for consecutive years, and which extends for a period of more than one year.

Such lease plans do not include an arrangement or agreement whereby a purchaser in exchange for an advance fee and yearly dues is entitled to select from a designated list of facilities located in more than one state accommodations, of companies which operate nationwide in at least nine states in the United States through franchises or ownership, for a specified time period and at reduced rates and under which no interest in real property is transferred

(10) "Vacation time sharing plan" means either a vacation time sharing ownership plan or a vacation time sharing lease plan as defined herein.

RELEVANT PARTS OF RESTATED AMENDED COMPLAINT

Primary Securities Claims against DH&S:

160B. DELOITTE AIDED AND ABETTED, AND PARTICIPATED AND CONSPIRED IN, THE LIFETIME PARTNERSHIP FRAUD, BY ITS CERTIFICATION OF PTL'S FINANCIAL STATEMENTS OF MAY 1984 AND NOVEMBER 1983 KNOWING OF THEIR FALSE AND MISLEADING NATURE AND BY EACH OF THE FOLLOWING 10 KNOWING OMISSIONS AND ACTS ("THE ACCOUNTANT AIDING AND ABETTING OR PARTICIPATION OR CONSPIRACY"), AS DESCRIBED IN DEPOSITIONS, MADDEN'S JULY 1989 EXPERT'S REPORT, AND PLAINTIFFS' NOVEMBER 24, 1989 BRIEF, ALL WITH CONSCIOUS INTENT AND IN VIOLATION OF GENERALLY ACCEPTED ACCOUNTING PRINCIPLES AND AUDITING STANDARDS (GAAP AND GAAS): (1) IT COVERED UP (OR MISREPRESENTED) LIFETIME PARTNERSHIP OVERSALES AND THE FALSITY OF PROMISES OF GREAT LIFETIME PARTNERSHIP VALUE; (2) IT COVERED UP (OR MISREPRESENTED) PTL'S INSOLVENCY AND APPARENTLY DESTROYED KEY DOCUMENTS; (3) IT MANAGED AND COVERED UP (OR MISREPRESENTED) THE SECRET BANK ACCOUNT AND WROTE ALL CHECKS (BUT DID NOT SIGN THEM); (4) IT COVERED UP (OR MISREPRESENTED) THE

LIFETIME PARTNER INVESTMENT DIVERSIONS; (5) IT ASSISTED AND COVERED UP (OR MISREPRESENTED) THE PRIVATE INUREMENT THAT CONSTITUTED THE FORMER OFFICER EMBEZZLEMENT; (6) IT COVERED UP (OR MISREPRESENTED) PTL'S TAX EXEMPTION LOSS; (7) IT COVERED UP (OR MISREPRESENTED) THE CONSTRUCTION EMBEZZLEMENT; (8) IT COVERED UP THE TIME SHARE LAW VIOLATIONS (DESCRIBED IN COUNTS 3-6); (9) IT COVERED UP THE SECURITIES LAW VIOLATIONS (DESCRIBED IN COUNTS 7-12); (10) IT COVERED UP THE INADEQUATE ACCOUNTING CONTROLS AND INADEQUATE AUDIT PROCEDURES. DELOITTE KNEW OF AND SUBSTANTIALLY ASSISTED, AND PARTICIPATED AND CONSPIRED IN, THE OMISSIONS AND MISREPRESENTATIONS, ON INFORMATION AND BELIEF. DELOITTE HAD A DUTY TO DISCLOSE THE OMISSIONS (OR ALTERNATIVELY THE MISREPRESENTATIONS) TO THE LIFETIME PARTNERS. OMISSIONS AND OTHER ACTS BY DELOITTE REFER TO JANUARY 1984 THROUGH MAY 1985 AND LATER CONSEQUENCES, AND EARLIER OMISSIONS AND ACTS WHEN AIDED AND ABETTED OR KNOWN BY DELOITTE AS PART OF CONSPIRACY.

. . . .

COUNT 7: FEDERAL SECURITIES LAWS FRAUD VIOLATIONS

370. Plaintiffs repeat and reallege all preceding allegations in this complaint.

(1) Antifraud Provision of Securities Act of 1933

371. The Former Officer Co-Conspirators and Messner & Company, with the substantial participation of DELOITTE AND LAVENTHOL . . ., "offer[ed] or s[old] a security (whether or not exempted . . .), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includ[ed] an untrue statement of a material fact or omit[ted] to state a material fact necessary in order to make the statements, in light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission)," and knew or in the exercise of reasonable care could have known of such untruth or omission, and thus are "liable to the person purchasing such security from [them]" (Securities Act of 1933 § 12(2), 15 U.S.C. § 77l(2)).

372. Said defendants offered and sold Lifetime Partnership Investments to the Lifetime Partners by mail, television, and telephone (the Lifetime Partnership Investment was described in Part III(A) and was incorporated herein by reference).

373. Said defendants made the Lifetime Partnership Promises in the Lifetime Partnership Offer and other mailed representations, and in other oral

representations by television and telephone. The foregoing representations contained the Material Misstatements and the Material Omissions (defined above).

374. The Lifetime Partners relied on the Lifetime Partnership Promises, including the Material Misstatements and Material Omissions. They did not then know of the untruths and omissions, and could not have known of them in the exercise of reasonable care. Such untruths and omissions were clearly material to the value of the Lifetime Partnership Investment.

375. The Lifetime Partners purchased the securities consisting of Lifetime Partnership Investments from the Former Officer Co-Conspirators and Messner & Company. Said defendants are liable to the Lifetime Partners.

375A. Bakker and Messner and some other Former Officer Co-Conspirators participated in the offers and sales by offering them by Bakker's letters, Bakker's and Messner's television appearances and offers, and other acts. The other Former Officer Co-Conspirators were substantial participants in the offers and sales by participating in strategy meetings, in offering material design, and in other acts, as well as aiding and abetting. Such defendants gained from the sales through the Former Officer Embezzlement and Secured Creditor Embezzlement.

375B. DELOITTE AND LAVENTHOL AUDITED AND CERTIFIED financial statements for PTL in connection with such

offers and sales without disclosing the securities and time share violations or the Foremer Officer Embezzlement and Secured Creditor Embezzlement, did not protest those violations to the PTL board and management or to the public or any governmental authority, in fact aided and abetted the Former Officer Co-Conspirators in those violations, and otherwise were substantial participants in the fraudulent sales process. DELOITTE AND LAVENTHOL gained from the sales through the receipt of accounting fees. DELOITTE AND LAVENTHOL, THROUGH THE ACCOUNTANT AIDING AND ABETTING OR PARTICIPATION OR CONSPIRACY, KNEW OF THE FOREGOING OMISSIONS AND MISREPRESENTATIONS AND ASSISTED THEM BY THEIR KNOWING AND/OR RECKLESS AND/OR CONSCIOUSLY INTENDED OMISSIONS AND ACTS DESCRIBED IN PARAGRAPHS 160B AND 160C.

375C. [INTENTIONALLY OMITTED.]

376. The Lifetime Partners bring this action within a year of when they discovered, or should have discovered in the exercise of reasonable care, the Material Misstatements and Material Omissions. That discovery could only occur after March 19, 1987 because relevant information was not reasonably available until the public revelations leading to Bakker's resignation, and in fact was covered up by the Former Officer Co-Conspirators, DELOITTE AND LAVENTHOL, Messner & Company, ...

(2) Antifraud Provisions of Securities Exchange Act of 1934

377. The Former Officer Co-Conspirators and Messner & Company, with the substantial participation of DELOITTE AND LAVENTHOL . . ., knowingly and intentionally "use[d] or employ[ed], in connection with the purchase or sale of any security . . ., any manipulative or deceptive device or contrivance in contravention of [SEC] rules and regulations" (Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(b)); and, "by the use of any means or instrumentality of interstate commerce, or of the mails," acted "(a) To employ any device, scheme, or artifice to defraud, (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances in which they were made, not misleading, or (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security" (Securities and Exchange Commission Rule 10b-5).

378. Said defendants sold, and the Lifetime Partners purchased, Lifetime Partner Investments that constitute securities (as described above).

379. Those offers and sales occurred by mail, television, and telephone.

380. Said defendants made the Lifetime Partnership Promises by the Lifetime Partnership Offer and other

written materials, and by oral statements on television and by telephone. Those promises and the Lifetime Partnership offers and sales contained the Material Misstatements and the Material Omissions (defined above), and thus said defendants knowingly and intentionally employed a device, scheme, or artifice to defraud, made material misstatements and material omissions, and engaged in acts or practices operating as a fraud and deceit on the Lifetime Partners. Said defendants had far greater access than did the offerees of the Lifetime Partnerships to relevant information, and knew and intended that such offerees would rely on the Material Misstatements and Material Omissions.

381. The foregoing fraudulent practices were engaged in in connection with the purchase and sale of securities, the Lifetime Partnerships.

382. The Lifetime Partners in fact relied on the Lifetime Partnership Promises, including the Material Misstatements and Material Omissions. Said defendants knew and intended that the Lifetime Partners would so rely.

383. Those misstatements and omissions caused the investment by the Lifetime Partners.

384. Said defendants acted with scienter, or an intent to defraud or reckless disregard for the truth of the statements and omissions made.

385. Said defendants are liable to the Lifetime Partners. Bakker and Messner and some other Former Officer Co-Conspirators participated in the offers and

sales by offering them by Bakker's letters, Bakker's and Messner's television appearances and offers, and other acts. The other Former Officer Co-Conspirators were substantial participants in the offers and sales by participating in strategy meetings, in offering material design, and in other acts, as well as aiding and abetting the fraudulent offers and sales. Such defendants gained from the sales through the Former Officer Embezzlement and Secured Creditor Embezzlement.

385A. DELOITTE AND LAVENTHOL AUDITED AND CERTIFIED financial statements for PTL without disclosing the securities and time share violations or the Former Officer Embezzlement and Secured Creditor Embezzlement, did not protest those violations to the PTL board and management or to the public or any governmental authority, in fact aided and abetted the Former Officer Co-Conspirators in those violations in general and also in the case of Laventhol & Horwath and Spears by maintaining fraudulent accounting practices and executing fraudulent transactions, and therefore intentionally engaged in a course of business which they knew would operate as a fraud on the Lifetime Partners in connection with their purchase of Lifetime Partnerships. DELOITTE AND LAVENTHOL gained from the sales through the receipt of accounting fees. DELOITTE AND LAVENTHOL, THROUGH THE ACCOUNTANT AIDING AND ABETTING OR PARTICIPATION OR CONSPIRACY, KNEW OF THE FOREGOING OMISSIONS AND MISREPRESENTATIONS AND

ASSISTED THEM BY THEIR KNOWING AND/OR RECKLESS AND/OR CONSCIOUSLY INTENDED OMISSIONS AND ACTS DESCRIBED IN PARAGRAPHS 160B AND 160C.

385B. [INTENTIONALLY OMITTED.]

386. The Former Officer Co-Conspirators and Messner & Company, to the extent not primarily liable under sections 12(2) and 10(b), are liable as controlling persons of PTL pursuant to Section 15 of the Securities Act of 1933 (15 U.S.C. § 77o) and Section 20(a) of the Securities Exchange Act of 1934 (15 U.S.C. § 78t). Each such defendant, either as officer, director, or confidant and co-conspirator with officers and directors, "possess[ed], direct[ly] or indirect[ly], . . . the power to direct or cause the direction of the management and policies" of PTL. (Securities and Exchange Commission Reg. C § 405). Such defendants had control of PTL and the fraudulent sale of Lifetime Partnerships "pursuant to or in connection with an agreement or understanding with one or more persons" (15 U.S.C. 77o), in that they all participated in the conspiracy with PTL management to effect the fraudulent sales.

387. The partial nonprofit organization exemption under securities laws, if applicable in this case, only provides exemption from certain registration requirements and not from the antifraud provisions of the securities laws.

388. Plaintiffs as the result of defendants'

wrongful actions have suffered the damages, and demanded the relief, described at the end of this complaint.

COUNT 8:NORTH CAROLINA SECURITIES ACT FRAUD VIOLATIONS

389. Plaintiffs repeat and reallege all preceding allegations in this complaint.

390. The Former Officer Co-Conspirators and Messner & Company, with the substantial participation of DELOITTE AND LAVENTHOL . . ., "offer[ed] or s[old] a security by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of the untruth or omission)," and knew or acted in reckless disregard of the untruth or omission, and thus are "liable to the person purchasing the security" from them (N.C.G.S. § 78A-56(a)(2)).

400. Because of the similarity of the foregoing section to Securities Act of 1933 § 12(2), section (1) of count 7 herein is incorporated herein by reference.

401. Secondary liability attaches under North Carolina common law and statute (N.C.G.S. § 78A-56(c)).

402. Plaintiffs as the result of defendants' wrongful actions have suffered the damages, and demanded the relief, described at the end of this complaint.

Negligence Claims against Directors and Officers for Permitting Securities Violations:

COUNT 15: NEGLIGENCE

440A. PLAINTIFFS REPEAT AND REALLEGE ALL PRECEDING ALLEGATIONS IN THIS COMPLAINT IN CONNECTION WITH BAKKER, TAGGART, AND CORTESE ONLY, IN THE ALTERNATIVE.

440B. BAKKER, TAGGART, AND CORTESE WERE NEGLIGENT IN THEIR CONDUCT AND/OR COMMITTED NEGLIGENT MISREPRESENTATION AND OMISSION, IN THEIR PTL ACTIVITIES AS DIRECTORS AND OFFICERS (I) IN CONNECTION WITH THE FOREGOING CONDUCT, TRANSACTIONS, AND OCCURRENCES (LIFETIME PARTNERSHIP FRAUD, DONOR FRAUD, FORMER OFFICER EMBEZZLEMENT, AND SECURED CREDITOR (CONSTRUCTION) EMBEZZLEMENT), AND (II) IN CONNECTION WITH VIOLATIONS OF THE FOREGOING STATUTES AND LEGAL RIGHTS (FEDERAL AND NORTH CAROLINA RICO, NORTH AND SOUTH CAROLINA TIMESHARE LAWS, FEDERAL AND NORTH AND SOUTH CAROLINA SECURITIES LAWS, AND NORTH AND SOUTH CAROLINA COMMON LAW FRAUD AND OTHER COUNT 13-14 STATUTES).

440C. SAID NEGLIGENCE AND/OR NEGLIGENT MISREPRESENTATION/OMISSION

CONSISTED OF THE FOLLOWING: (I) CORTESE, BAKKER, AND TAGGART OWED A DUTY OF CARE AND OTHER FIDUCIARY DUTIES TOWARD THE LIFETIME PARTNERS, TOWARD PTL, AND TOWARD THEIR RESPONSIBILITIES AS DIRECTORS AND/OR OFFICERS OF PTL; (II) THEY VIOLATED THOSE DUTIES BY MOST OR ALL OF CORTESE'S MATERIAL ACTIONS AND OMISSIONS, AND SOME OF BAKKER'S AND TAGGART'S MATERIAL ACTIONS AND OMISSIONS, INCLUDING WITHOUT LIMITATION NOT DISCOVERING OR CORRECTING LIFETIME PARTNERSHIP FRAUD, DONOR FRAUD, FORMER OFFICER EMBEZZLEMENT, AND SECURED CREDITOR (CONSTRUCTION) EMBEZZLEMENT; (III) CORTESE'S, BAKKER'S, AND TAGGART'S NEGLIGENT ACTIONS AND OMISSIONS PROXIMATELY CAUSED INJURY TO THE LIFETIME PARTNERS, WHO WERE INDUCED TO INVEST IN LIFETIME PARTNERSHIPS AND THEN DEPRIVED OF THE BENEFITS OF THOSE PARTNERSHIPS, WHO JUSTIFIABLY RELIED ON BAKKER'S, TAGGART'S, AND CORTESE'S PROPER DISCHARGES OF THEIR DUTIES, AND WHOSE RELIANCE WAS REASONABLY FORESEEABLE;

440D. SAID NEGLIGENCE AND/OR NEGLIGENT MISREPRESENTATION/OMISSION VIOLATED NORTH CAROLINA STATUTES AND COMMON LAW, AND SOUTH CAROLINA STATUTES AND COMMON LAW.